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## **RiskMetrics Group Discloses Complete Methodology of Governance Risk Indicators (GRId)**

In our March 3, 2010, alert letter *RiskMetrics Group Releases Governance Risk Indicators (GRId) Tool to Measure Governance-Related Risk*<sup>1</sup> we announced that RiskMetrics Group (formerly Institutional Shareholder Services, or ISS) recently introduced Governance Risk Indicators (GRId), a new tool for institutional investors to assess the level of governance-related risk at current or prospective portfolio companies. On March 10, 2010, RiskMetrics released a technical document outlining the complete GRId methodology, including all the questions, scorings, and weightings for each applicable market. This letter is a follow-up to our March 3 letter to provide further detail on the GRId methodology and potential implications, particularly as they relate to executive compensation.

### **GRId Methodology**

GRId uses the same principles underlying RiskMetrics' corporate governance policies for developing proxy voting recommendations to model governance-related risk. GRId ratings are determined on an absolute basis compared to "best practices" rather than on a relative basis compared to peer and general industry practices. "Best practices" are aligned with RiskMetrics' proxy voting policies and will be updated annually in connection with updates to RiskMetrics' proxy voting policies. GRId measures the level of risk in the following four governance categories at three different "concern" levels (low, medium, and high, which are color-coded, respectively, as blue, yellow, and red):

1. Audit
2. Board
3. Shareholder Rights
4. Compensation

GRId assesses the governance risk in the four categories based on questions tailored to the governance practices of each market covered. Each category is divided into subcategories, with questions addressing risk-related topics for each subcategory. The 63 questions applicable to U.S. companies are contained in the Attachment, along with the weightings and scoring system. Scores for each of the four governance categories are normalized on a scale of 0-100 for ease of understanding and comparability.

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<sup>1</sup> *RiskMetrics Group Releases Governance Risk Indicators (GRId) tool to Measure Governance Related Risk*, March 3, 2010 ([http://www.fwcook.com/alert\\_letters/03-3-10\\_RiskMetrics\\_Group\\_Releases\\_Governance\\_Risk\\_Indicators\\_%28GRId%29\\_Tool\\_to\\_Measure\\_Governance-Related\\_Risk.pdf](http://www.fwcook.com/alert_letters/03-3-10_RiskMetrics_Group_Releases_Governance_Risk_Indicators_%28GRId%29_Tool_to_Measure_Governance-Related_Risk.pdf))

The table below indicates the scores for U.S. companies converted to levels of concern. Similar tables are customized to each market (e.g., Canada, Europe).

U.S. Concern Level	Score Range			
	Audit	Board	Shareholder Rights	Compensation
High	0-75	0-55	0-35	0-55
Median	75-90	55-70	35-60	55-70
Low	90-100	70-100	60-100	70-100

Companies will be able to verify their data prior to the publication of the initial ratings on the GRId Data Verification site (see “GRId Data Verification” in the “Additional GRId-Related Tool” section below). RiskMetrics will send each company an email once its data are available for review, and each company will be provided a limited timeframe to verify its data. If any errors are found after a proxy report has been published prior to the shareholder meeting, RiskMetrics will issue a revised proxy report. The schedule for the release of official GRId scores depends on the date of the company’s annual meeting. If the annual meeting is held in April or May 2010, the official GRId score will be published on RiskMetrics’ Proxy Analysis report for that shareholders meeting. For companies with annual meetings prior to April or after May, the first official pre-score will be available by June 30, 2010.

### **GRId Compensation Category**

In total GRId’s Compensation category comprises 65 questions divided into 13 subcategories, but not all questions are applicable in all markets. For U.S. companies, there are 28 questions divided into eight subcategories as follows:

1. Executive Short Term
  - a. Performance (1)
2. Executive Long Term/Equity
  - a. Performance (4)
  - b. Dilution (2)
  - c. Timing (4)
  - d. Other (2)
3. Other
  - a. Stock Ownership (4)
  - b. Termination (1)
  - c. Pay Practices (10)

While most of the questions and scorings are consistent with RiskMetrics’ proxy voting guidelines and general corporate governance “best practices,” there are some nuances worth highlighting:

1. The single most important question based on weighting pertains to the severance trigger under change-in-control agreements. This question accounts for 22.75% of the entire compensation category, while all other questions each account for 5% or less. A company with no agreements or a double trigger would score a (+3); a company with a

modified single trigger in an agreement that was neither entered into nor amended in the last year would score a (-3), and a company that does not disclose its trigger or that has a single or modified trigger in an agreement that was either entered into or amended in the last year would score a (-5). Therefore, GRId will penalize companies having a single or modified trigger provision in an old agreement, which is more severe than RiskMetrics' proxy voting guidelines.

2. GRId penalizes companies that provide excise tax gross-ups related to change-in-control payments. If the gross-up provision is in an agreement that was neither entered into nor amended in the last year a score of (-3) would apply, if the gross-up provision is in an agreement that was either entered into or amended in the last year a score of (-5) would apply, and companies that do not provide an excise tax gross-up will receive a neutral (0). Therefore, like the severance trigger, GRId penalizes companies having an excise tax gross-up provision in an old agreement, which is more severe than RiskMetrics' proxy voting guidelines.
3. GRId penalizes companies that do not disclose information on annual bonuses, including performance measures (a score of (-5) will apply), but GRId does not penalize companies for not having performance-vesting long-term incentives, such as performance shares or performance cash. In fact, if a company has a performance-vesting long-term incentive, but does not disclose the specific performance measures, it will still receive a positive score of (+2.5) (a score of (0) will apply to long-term cash plans).
4. It is in a company's best interest to disclose whether or not executives are subject to equity holding periods, as nondisclosure will penalize the company (a score of (-3) will apply). If it is disclosed that executives are not subject to a holding period a neutral score of (0) will apply, and if executives are subject to a holding period a positive score will apply, with hold-until-retirement or longer scoring (+5), the highest possible score.
5. GRId distinguishes between "robust", "standard", and "substandard" CEO and director stock ownership guidelines, which will receive a score of (+3), (0), and (-3), respectively. GRId defines robust guidelines as greater than five times salary or retainer, standard as three to five times salary or retainer, and substandard as less than three times salary or retainer. Nondisclosure of ownership guidelines will receive a (-5), the lowest possible score.

For a complete list of all the questions including the scoring and weightings, please refer to the [Attachment](#).

### **Additional GRId-Related Tools**

In connection with the release of GRId, RiskMetrics has released the following four "GRId Solutions":

1. [GRId Data Verification](#) – This tool is available at no cost to all companies covered by GRId, and will allow each company to check the accuracy of its data, request changes to the data, and view GRId indicators which will be updated monthly. For more information, visit [http://www.riskmetrics.com/data\\_verification](http://www.riskmetrics.com/data_verification).

2. Governance Exchange – This tool, available for a fee, is an online platform with discussion forums and a range of corporate governance viewpoints and information sources, including webcasts, white papers, surveys, and expert analyses. Corporate issuers also have integrated access to RiskMetrics’ core governance tools, GRId Analytics (see below), GRId Pre-Scoring (see below), Voting Analytics, and Resource Center. In addition, the platform will provide access to corporate advisors that specialize in providing data, analytics and reports to executives and board members. For more information, visit [http://www.riskmetrics.com/governance\\_exchange/issuers](http://www.riskmetrics.com/governance_exchange/issuers).
3. GRId Analytics – This tool, available for a fee, provides access to new modeling and analytical tools relating to the new GRId methodology, such as “what if” scenarios, peer comparisons, new tear sheet GRId reports, new customized reports showcasing your company’s corporate governance strengths, the ability to drill down into the database to identify trends, insights into peer practices, and a dedicated advisor. For more information, visit [http://www.riskmetrics.com/benchmarking/GRId\\_analytics](http://www.riskmetrics.com/benchmarking/GRId_analytics).
4. GRId Pre-Scoring – This tool is available to subscribers to RiskMetrics’ Governance Exchange, and will allow companies to obtain unofficial GRId pre-scores.

### **Potential Implications**

GRId’s scoring approach, which penalizes companies more for nondisclosure of certain items than for the existence of problematic pay practices, will serve to encourage full disclosure of all corporate governance practices.

As mentioned in our previous letter, it is important to keep in mind that RiskMetrics will not use the new GRId ratings as a determinant for its proxy voting recommendations, but will continue to use the underlying corporate governance policies upon which the ratings will be based. Therefore, a “low risk” GRId rating will not guarantee a positive vote recommendation from RiskMetrics, and vice versa, as a company with a poor governance practice (e.g., a new change-in-control severance agreement with a single-trigger provision) that otherwise only has “best practices” could still receive a negative vote recommendation despite receiving a “low risk” GRId rating.

Visit [www.riskmetrics.com/grid-info](http://www.riskmetrics.com/grid-info) for more information on GRId, including the complete technical document, a list of FAQs for corporate issuers and institutional investors, and a sample GRId profile.

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General questions about this letter can be addressed to Katrin Cox in our Chicago office at (312) 894-0076 or [klcox@fwcook.com](mailto:klcox@fwcook.com) or Wendy Hilburn in our New York office at (212) 299-3707 or [wjhilburn@fwcook.com](mailto:wjhilburn@fwcook.com). Copies of this letter and other published materials are available on our website, [www.fwcook.com](http://www.fwcook.com).

**GRId Questions, Weightings, and Scoring for U.S.-Based Companies**

<b>Audit (6 questions)</b>		
<i>(% Weighting)</i>		<i>(Scoring: 5 = best practice; 0 = neutral, -5 = poor practice)</i>
<b>21.25% Non-Audit Fees (1 question)</b>		
21.25%	Non-Audit fees represent what percentage of total fees?	<b>0</b> <= 50% of total fees <b>-5</b> > 50% of total fees / Not disclosed
<b>57.50% Controversies (4 questions)</b>		
21.25%	Did the auditor issue an adverse opinion in the past year?	<b>0</b> Unqualified opinion / going concern determination <b>-3</b> Qualified opinion <b>-5</b> Adverse opinion
10.00%	Has the company restated financials for any period within the past two years?	<b>0</b> No <b>-5</b> Yes
5.00%	Has the company made late financial disclosure filings in the past two years?	
21.25%	Has a securities regulator taken enforcement action against the company in the past two years?	
<b>21.25% Other Issues (1 question)</b>		
21.25%	Has the company disclosed any material weaknesses in its internal controls in the past two years?	<b>0</b> No / Not disclosed <b>-1</b> Yes, in the previous fiscal year only <b>-2</b> Yes, in most recent fiscal year only <b>-3</b> Yes, both years, but different material weakness  <b>-5</b> Yes, both years, same weakness in consecutive years

<b>Board Structure (14 questions)</b>		
<i>(% Weighting)</i>		<i>(Scoring; 5 = best practice; 0 = neutral, -5 = poor practice)</i>
<b>25.00% Board Composition (2 questions)</b>		
15.00%	What is the independent director composition of the board?	<b>0-+5</b> > 50% independent (linear interpolation; 50% = <b>0</b> , 100% = <b>+5</b> ) <b>-5</b> <= 50% independent
10.00%	What is the qualification of the Chairman of the Board?	<b>+5</b> Independent director <b>0</b> Separate lead director (no chairman) <b>-5</b> Executive director or non-independent non-executive director / No information
<b>15.00% Committee Composition (3 questions)</b>		
5.00% <sup>(1)</sup>	What is the independent <sup>(2)</sup> status of the nominating committee members?	<b>0-+5</b> >= 50% independent <sup>(2)</sup> (linear interpolation; 50% = <b>0</b> , 100% = <b>+5</b> ) <b>-5</b> < 50% independent <sup>(2)</sup>
5.00% <sup>(1)</sup>	What is the independent <sup>(2)</sup> status of the compensation committee members?	
5.00% <sup>(1)</sup>	What is the independent <sup>(2)</sup> status of the audit committee members?	
<b>60.00% Board Practices (9 questions)</b>		
8.95%	Does the CEO serve on an excessive number of outside boards?	<b>0</b> CEO serves on 2 or less outside boards / Not disclosed <b>-5</b> CEO serves on 3 or more outside boards
9.95%	Do non-executives serve on an excessive number of outside boards?	<b>0</b> No directors serve on 7 or more outside boards <b>-5</b> At least 1 director serves on 7 or more outside boards / Not disclosed
4.28%	Did any directors attend less than 75% of the board meetings without a valid excuse?	<b>+5</b> No <b>-5</b> Yes / Not disclosed
3.98%	Does the company disclose board/governance guidelines?	<b>+5</b> Yes <b>-5</b> No
3.98%	Did outside directors meet without management present?	<b>+5</b> Yes <b>-5</b> No / Not disclosed
9.95%	How many directors received withhold / against votes of 50% or greater at the last annual meeting?	<b>0</b> None <b>-3</b> 1 director <b>-5</b> 2 or more directors / Not disclosed
6.97%	What percent of the directors were involved in material related party transactions (RPTs)?	<b>0</b> <= 50% of directors <b>-5-0</b> > 50% of directors (linear interpolation; 50% = <b>0</b> , 100% = <b>-5</b> )
1.99%	Do the directors with related party transactions (RPTs) sit on key board committees?	<b>+5</b> No / Not applicable <b>-5</b> Yes / Not disclosed
9.95%	Does the company have a majority vote standard in uncontested elections?	<b>+5</b> Yes; company has a director resignation policy <b>0</b> Yes; company does not have a director resignation policy <b>-3</b> No; company has a plurality vote standard and a director resignation policy <b>-5</b> No; company has a plurality vote standard and no director resignation policy

<sup>(1)</sup> All committees are weighted equally, however, the weighting is doubled for any questions where the score is negative.

<sup>(2)</sup> As defined by RiskMetrics.

<b>Shareholder Rights (15 questions)</b>		
<i>(% Weighting)</i>	<i>(Scoring: 5 = best practice; 0 = neutral, -5 = poor practice)</i>	
<b>10.00% One Share One Vote (2 questions)</b>		
5.00%	Does the company have classes of stock with different voting rights?	0 No
5.00%	Are there any directors on the board who are not up for election by all classes of common shareholders?	-5 Yes
<b>50.00% Takeover Defenses (7 questions)</b>		
16.67%	Are all directors elected annually?	+5 Yes 0 Company is transitioning to annual elections -5 No
16.67%	Does the company have a poison pill (shareholder rights plan) that was not approved by shareholders?	0 No -5 Yes
<sup>(3)</sup>	What is the trigger threshold for the poison pill?	0 >= 50% / Net Operation Loss Pill -5-0 < 50% (linear interpolation; 50% = 0, 20% = -5) -5 < 20%
<sup>(3)</sup>	Does the poison pill have a sunset provision?	
<sup>(3)</sup>	Does the poison pill have a Three-Year Independent Director Evaluation (TIDE) provision?	+5 Yes -5 No
<sup>(3)</sup>	Does the poison pill have a qualified offer clause?	
6.36%	Is the board authorized to issue blank check preferred stock?	+5 No 0 Only under "declaw" provision / Not applicable -5 Yes
<b>17.00% Voting Issues (3 questions)</b>		
6.80%	Does the company require a super-majority vote to approve amendments to the charter and bylaws?	+5 No 0 Not disclosed -5 Yes
6.80%	Does the company require a super-majority vote to approve mergers/business combinations?	+5 No (not a controlled company) 0 Not disclosed -2 No (controlled company) -5 Yes
3.40%	When does the shareholder rights plan expire?	+3 < 3 years 0 > 3 years / Not applicable
<b>23.00% Voting Formalities (3 questions)</b>		
4.60%	What is the percentage of share capital needed to convene a special meeting?	+5 <= 10% -5 > 10% / No right to call a special meeting
2.30%	Can shareholders act by written consent?	+5 Yes 0 Not disclosed -5 No
16.10%	Has the board failed to implement a shareholder resolution supported by a majority vote?	0 No / Not applicable -5 Yes; board has ignored majority support of outstanding shares over one year or majority support of votes cast over two years

<sup>(3)</sup> Weightings tied to scores for these questions will vary based on whether the company has a poison pill. If there is no poison pill, weightings will be zero and weights tied to other subsection questions will scale up proportionately.

<b>Compensation/Remuneration (28 questions)</b>	
<i>(% Weighting)</i>	<i>(Scoring: 5 = best practice; 0 = neutral, -5 = poor practice)</i>
<b>3.00% Executive Short Term (1 question)</b>	
3.00% Does the company disclose the performance measures, hurdle rates, and target payout thresholds for the short-term cash incentive plan that generated the awards reported?	<b>+5</b> Company discloses complete information <b>0</b> Not applicable / Company discloses general performance measure(s) without further information <b>-5</b> No information on variable performance related payment or on general performance measure
<b>32.00% Executive Long Term/Equity (12 questions)</b>	
<b>Performance</b>	
1.60% Does the company disclose a performance measure for stock options plans (for executives)?	<b>+5</b> Grant based on disclosed peer group; positioning of company disclosed / Grant based on disclosed target
1.60% Does the company disclose a performance measure for restricted share plans (for executives)?	<b>+2.5</b> Company discloses general performance measure(s) without further information / Grant based on undisclosed peer group and positioning of company is not disclosed / Grant based on undisclosed target <b>0</b> No information / Not applicable / No performance conditions
1.60% Does the company disclose the performance measures, hurdle rates and target payout thresholds for executives' long-term cash plans?	<b>+5</b> Company discloses complete information <b>0</b> No information on variable performance related payout or general performance measures / Not applicable / Company discloses general performance measure(s) without further information
1.60% Does the company disclose a performance measure for other long term plans (for executives)?	<b>+5</b> Grant based on disclosed peer group; positioning of company disclosed <b>+2.5</b> Grant based on undisclosed peer group and positioning of company is not disclosed <b>0</b> No information / Not applicable / No performance conditions / Company discloses general performance measure(s) without further information / Target-based grant
<b>Dilution</b>	
1.60% Does at least one of the new and/or amended plans for the last three years permit share recycling for options/SARS?	<b>+5</b> No <b>0</b> Not Applicable <b>-5</b> Yes
4.80% Does the company grant equity awards at an excessive rate, according to RMG policy?	<b>+5</b> Average annual burn rate over the past three fiscal years is 2% or less, or within one standard deviation of the industry mean <b>0</b> Average annual burn rate over the past three fiscal years greater than 2% and exceeds one standard deviation of the industry mean, but company has made a commitment to keep the burn rate within one of these thresholds in the future / Not applicable / Company coming out of bankruptcy or public less than 3 years <b>-5</b> Average annual burn rate over the past three fiscal years greater than 2% and exceeds one standard deviation of the industry mean



<b>Compensation/Remuneration (28 questions)</b>	
<i>(% Weighting)</i>	<i>(Scoring: 5 = best practice; 0 = neutral, -5 = poor practice)</i>
<p><b>Timing</b></p> <p>2.40% What are the minimum vesting periods mandated in the plan documents for executives' stock options or SARS in the equity plans adopted/amended in the last 3 years?</p> <p>2.40% What are the minimum vesting periods mandated in the plan documents, adopted/amended in the last three years, for executives' restricted stock?</p>	<p><b>+3</b> 5 years or more</p> <p><b>+2</b> 4 years</p> <p><b>+1</b> 3 years</p> <p><b>0</b> Not Applicable / Not disclosed / 1-2 years</p>
<p>2.40% What is the holding period for stock options (for executives)?</p> <p>2.40% What is the holding period for restricted shares (for executives)?</p>	<p><b>+5</b> End of employment or beyond</p> <p><b>+3</b> &gt;= 2 years</p> <p><b>0-+3</b> &lt; 2 years (linear interpolation; 0 years = <b>0</b>, 2 years = <b>+3</b>)</p> <p><b>0</b> Not applicable</p> <p><b>-3</b> Not disclosed</p>
<p><b>Other</b></p> <p>4.80% Does one or more of the company's equity plans approved or amended in the past three years permit option/ SAR repricing and cash buyouts?</p>	<p><b>+5</b> All plans expressly forbid option repricings and cash buyouts</p> <p><b>+3</b> Plans prohibit repricing, but are silent on cash buyouts</p> <p><b>0</b> Not Applicable</p> <p><b>-3</b> Not disclosed</p> <p><b>-5</b> Yes</p>
<p>4.80% Has the company repriced options or exchanged them for shares, options or cash without shareholder approval in the last three years?</p>	<p><b>+5</b> No</p> <p><b>-5</b> Yes</p>
<b>65.00% Other (15 questions)</b>	
<p><b>Stock Ownership</b></p> <p>2.44% If a new or amended broad-based plan is proposed, then what is the expected duration of shares?<sup>(4)</sup></p>	<p><b>+3</b> &lt;= 4 years</p> <p><b>+3--3</b> 4 - 7 years (linear interpolation; 4 years = <b>+3</b>, 7 years = <b>-3</b>)</p> <p><b>-3</b> &gt;= 7 years</p> <p><b>0</b> Not applicable</p>
<p>2.44% Is the CEO subject to stock ownership guidelines?</p> <p>2.44% Are directors subject to stock ownership guidelines?</p>	<p><b>+3</b> Yes, &gt; 5x salary/retainer ("robust")</p> <p><b>0</b> Yes, 3x-5x salary/retainer ("standard")</p> <p><b>-3</b> Yes, &lt; 3x salary/retainer ("substandard")</p> <p><b>-5</b> Not disclosed</p>
<p>2.44% Do all directors with more than one year of service own stock?</p>	<p><b>+3</b> Yes</p> <p><b>-5</b> No / Not disclosed</p>
<p><b>Termination</b></p> <p>22.75% What's the severance trigger under the change-in-control agreements?</p>	<p><b>+3</b> No agreements / Double trigger</p> <p><b>-3</b> Modified single trigger but agreement was neither amended nor entered into the last year</p> <p><b>-5</b> Single trigger / Not disclosed / Modified single trigger in agreement that was amended or entered into the last year</p>

<sup>(4)</sup> Duration is estimated by dividing the number of new shares proposed to be added plus shares available under an equity compensation program by the estimated annual share usage under an equity compensation program. The estimated annual shares usage is determined by multiplying the company's unadjusted three-year average burn rate (number of shares subject to time-based awards granted divided by weighted common shares outstanding during the past three fiscal years divided by three) by the company's most recent weighted common shares outstanding.

<b>Compensation/Remuneration (28 questions)</b>	
<i>(% Weighting)</i>	<i>(Scoring: 5 = best practice; 0 = neutral, -5 = poor practice)</i>
<b>Pay Practices</b>	
3.25% Did the company disclose a claw back provision?	+3 Yes -3 No
3.25% Are any of the NEOs eligible for multi-year guaranteed bonuses?	0 No -5 Yes
3.25% Do any of the NEOs receive tax gross-ups on their perks other than relocation and other broad-based benefits?	+5 No 0 Yes, but company is committing to discontinue or end gross-ups -5 Yes
3.25% What is the multiple of salary plus bonus in the change-in-control agreements for named executive officers excluding the CEO?	+5 No severance agreements 0 3x or less; bonus is defined as target or actual
3.25% What is the multiple of salary plus bonus in the severance agreements for the CEO upon a change-in-control?	-5 > 3x / Bonus is defined as maximum or greater of actual and maximum / Not disclosed
3.25% Does the company provide excise tax gross-ups for change-in-control payments?	0 No / Company has committed to remove gross-up provision -3 Yes; applicable agreements were neither entered into nor materially amended within past year -5 Yes; applicable agreements were entered into or materially amended within past year
3.25% What is the length of the employment agreement with the CEO?	+5 No agreement 0 Not disclosed +3 < 3 years +3--1 3-4 years (linear interpolation; 3 years = +3, 4 years = -1) -1--5 4-10 years (linear interpolation; 4 years = -1, 10 years = -5) -5 >= 10 years / Auto-renewal
3.25% Are executives given credit toward pension for years not worked?	0 No -5 Yes
3.25% In the last fiscal year, did the company grant premium priced options of at least 125% of market price that need to be maintained for at least 30 consecutive days?	+5 Yes +3 Yes, but company is silent on sustainability of stock price 0 No
3.25% Has the company voluntarily adopted a management 'say on pay' advisory vote resolution for the most recent annual meeting or committed to a resolution going forward?	+5 Voluntary adopter 0 No; company was not subject to shareholder say-on-pay proposal -5 No; company was subject to shareholder say-on-pay proposal which received majority approval