Appendix A

1. Gompers, Ishii and Metrick G Index

Groupings of IRRC governance provisions:

1. “Delay.” Four provisions intended to delay hostile takeover bidders (the presence of blank check preferred stock or a classified board, and restrictions on shareholders’ ability to call special meetings or to act by written consent).

2. “Voting.” Six provisions dealing with shareholder voting rights (the presence of cumulative voting, confidential voting, supermajority voting for business combinations, dual class stock, and limitations to shareholders’ ability to amend the bylaws or certificate of incorporation).

3. “Protection.” Six provisions protecting directors and officers from legal liability or job termination (limited liability provisions, indemnification provisions in charters or bylaws, indemnification contracts, golden parachutes, severance contracts not conditioned on control changes, and compensation plans with changes-in-control provisions).

4. “Other.” The six remaining provisions related to takeover defenses (the presence of antigreenmail provisions, fair price provisions, other constituent provisions, poison pills, silver parachutes, and pension parachutes).

5. “State.” Six state takeover laws (antigreenmail, business combination freeze, control share acquisition, fair price, other constituencies and redemption rights statutes).

Note that these groupings can be questioned for lack of internal coherence. For example, blank check preferred, which they classify in the “delay” category is used in the creation of poison pills, yet poison pills are placed in the “other” category.
2. Bebchuk, Cohen and Ferrell Entrenchment Index

   Subset of G index used (Gompers et al.’s group classification in parentheses):
   
   1. Classified boards (Delay)
   2. Limitations to shareholders’ ability to amend the bylaws (Voting)
   3. Supermajority voting for business combinations (Voting)
   4. Supermajority requirements for charter amendments (Voting)
   5. Poison pills (Other)
   6. Golden parachutes (Protection)

3. Brown and Caylor Gov-Score

   ISS groupings, factors ordered by proportion of firms with minimally accepted standard

   (factors in Gompers et al. G score are in italics):
   
   1. Audit. Four factors: audit committee consists solely of independent outside directors; auditors ratified by shareholders at most recent annual meeting; consulting fees paid to auditors less than audit fees paid; company has formal policy on auditor rotation
   2. Board of directors. 17 factors: managers respond to shareholder proposals within 12 months of meeting; CEO serves on no more than two other public corporation boards; all directors attended at least 75% of board meetings or had valid excuse for non-attendance; size of board between 6 and 15; no former CEO is a director; no CEO related-party transactions listed in proxy; board has more than 50% independent outside directors; compensation committee comprised solely of independent outside directors; CEO and Chairman positions are separated or lead director is specified; shareholders vote on directors selected to fill vacancies; annual director elections; shareholder approval to
change board size; nominating committee comprised solely of independent outside directors; governance committee meets at least once a year; *cumulative voting rights*; board guidelines in proxy statement; policy requiring outside directors to serve on no more than five additional boards

3. Charter/bylaws. Seven factors: *majority vote for merger; no poison pill or shareholder approved pill; shareholders can call special meetings; majority vote to amend charter or bylaws; shareholders may act by nonunanimous written consent; no blank check preferred stock; board cannot amend bylaws without shareholder approval or can do so only under limited circumstances*

4. Director education. One factor: at least one director has participated in ISS-accredited director education program

5. Executive and director compensation. Ten factors: no interlocking directors on compensation committee; non-employees do not participate in pension plans; no option repricing in past three years; shareholder approval of stock incentive plans; directors receive all or part of fees in stock; no corporate loans to executives to exercise options; last time shareholders voted on a pay plan ISS did not deem the cost to be excessive; average options granted in past three years as percentage of basic shares outstanding no more than 3 percent (“option burn rate”); prohibition on option repricing; expenses stock options

6. Ownership. Four factors: all directors with more than one year of service own stock; officers’ and directors’ stock ownership at least 1 percent and not over 30%; executives subject to stock ownership guidelines; directors subject to stock ownership guidelines
7. Progressive practices. Seven factors: mandatory retirement age for directors; board performance regularly reviewed; board-approved CEO succession plan in place; board has outside advisors; directors must submit resignation upon change in job status; outside directors meet without CEO and disclose number of times they meet; director term limits

8. State of incorporation. One factor: incorporation in state with no takeover statutes

Note that all of the factors in ISS’s charter/bylaw grouping are also in the G index; the remaining G index components included in Gov-Score are in the board of directors category. In addition, while Brown and Caylor do not identify the state of incorporation factor as in the G index, and so it is not in italics in the above list, it is essentially a composite of the four components in Gompers et al.’s “state” grouping.

The seven factors that Brown and Caylor identify in their 2005 paper as driving the original results and the grouping (in parentheses) into which they fall are as follow (italicized provisions also in Bebchuk et al. entrenchment index):

1. annual director elections (Board of directors)
2. no poison pill or shareholder approved pill (Charter/bylaws)
3. no option repricing in past three years (Executive and director compensation)
4. average options granted in past three years as percentage of basic shares outstanding no more than 3 percent (Executive and director compensation)
5. all directors attended at least 75% of board meetings or had valid excuse for non-attendance (Board of directors)
6. board guidelines in proxy statement (Board of directors)
7. directors subject to stock ownership guidelines (Ownership)
4. The Corporate Library Board Effectiveness Rating

Components in the rating:

1. Board Composition. Described as the only component not based primarily on board actions and decision-making, and related to an analysis of the historical governance patterns of firms that experienced governance failures, it consists of screens on director tenure, age, and independence, the number of active or former CEOs on the board, and whether a past CEO is chairman, and director “over-commitment” (sitting on more than four other boards)

2. CEO Compensation. Depends on the balance of fixed and variable pay, how much variable pay is in the form of stock, with numerical red flags, such as base salary over $1 million, “excessive” options and high perquisite payments, and disclosure practices.

3. Shareholder Responsiveness. History of board’s response to successful shareholder proposals (those receiving a majority of the votes).

4. Litigation & Regulatory Problems. Based on the incidence of litigation and assessed fines, includes an evaluation of the amount of disclosure of current or potential liability exposure, and the existence of repeated regulatory infractions or fines.

5. Takeover Defenses. Detailed information provided on defenses, with better ratings assigned for unidentified “more shareholder friendly” defenses.

6. Accounting. Screen compares current quarter reports against prior four quarters for indicators of potential earnings management or other accounting concerns.

7. Strategic Decisionmaking. Focuses on board approval of mergers and acquisitions (with lower ratings assigned to approvals of mergers resulting in significant loss of
shareholder value).

8. Analyst Adjustment. Analyst may adjust the board rating up or down for reasons that fall outside the regular scoring system.

The first two components, board composition and CEO composition, comprise half of the overall rating, with equal weights applied to the other five governance components. The analyst adjustment is described as “determined on an individual basis.”

The Corporate Library’s Best Practices Compliance Score is based on the following factors:

whether the firm has a classified board, majority outside directors, independent chairman or lead director, audit committee of only independent directors, formal governance policy, and the number of directors who are over 70 years old, serve on more than 4 other boards and have more than 15 years of service.

5. GovernanceMetrics International Market and Industry Indices

Research Categories:

1. Board Accountability
2. Financial Disclosure and Internal Controls
3. Shareholder Rights
4. Executive Compensation
5. Market for Control and Ownership Base
6. Corporate Behavior and Corporate Social Responsibility Issues

6. ISS Corporate Governance Quotient

Governance Areas and Weights
1. Board of directors - 40%
2. Compensation - 30%
3. Takeover defenses - 20%
4. Audit - 10%

The eight most important governance variables that enter into the rating, in order of their weighting are:

- audit committee with all independent outside directors; average options granted in past three years as percentage of basic shares outstanding no more than 2 percent or less or within one standard deviation of industry mean (“option burn rate”); all audit committee members are financial experts; board controlled by supermajority (over 90%) of independent outside directors; board has only one non-independent director; directors subject to stock ownership requirements; board controlled by supermajority (between 75 - 90%) of independent outsiders; incorporation in state with no takeover statutes

The sixteen performance measures ISS used to test its governance rating factors, which are divided into four categories of performance, are as follow:

1. Risk. Two measures: Volatility; Altman’s Z score (probability of bankruptcy)
2. Market. Two measures: Total Shareholder Return; Tobin’s Q
3. Valuation. Three ratio measures: Price to Book; Price to Cash Flow; Price to Earnings
4. Profitability. Nine measures: Dividend; Return on Invested Capital; Return on Equity; Return on Investment; Cash Flow Return in Investment; Net Profit Margin; EBITDA Margin; Sales Growth; Free Cash Flow to Sales