The Voice for Public Pensions

NCPERS VOTING GUIDELINES

I. Introduction

A. This document sets forth guidelines regarding the voting of proxies for the equity investments of the ______________________________________ ("Plan").
B. These guidelines reflect the Plan's determination of what positions are in the best economic interests of its beneficiaries on the most common and recurring proxy issues.
C. The Plan directs its proxy voting agent ("agent") to follow these guidelines unless the agent, using the care, skill, prudence and diligence that a prudent person would under the prevailing circumstances, believes that the agent should depart from these guidelines to protect the best economic interest of the Plan's beneficiaries. In such circumstances, the agent should advise the Plan, in advance of the proxy vote deadline, of the agent's intentions to depart from these guidelines and the agent's specific reasons for doing so. The Plan reserves the authority to direct the agent to vote the Plan's proxies in accordance with these guidelines.
D. If these guidelines do not apply, either directly or by reasonable interpretation, to a proxy issue, or if the guidelines acknowledge that the issue must be decided on a case-by-case basis, the agent is directed to use the care, skill, prudence and diligence that a prudent person would under the prevailing circumstances to cast a vote in the economic best interests of the Plan's beneficiaries.

II. Management Proposals

A. Routine Election of Board of Directors.

1. Two-thirds of the board of directors should be made up of independent outsiders. A director is not independent if he/she is a current or former employee or officer of the company, a relative of a current or former employee or officer, a person who has or had a business relationship with the company (e.g., lawyer, consultant, vendor, buyer), is part of an interlocking directorate (i.e., the director is employed by another corporation and an executive officer of the company serves on that other corporation's board), or owns such a substantial amount of company shares that he/she is viewed as controlling the company. If two-thirds of the board of directors is not represented by independent outsiders, a vote should be cast to withhold authority for all nominees who are insiders.

2. A company’s nominating, compensation and audit committees should be made up entirely of independent outsiders. If they are not, a vote should be cast to withhold authority from all nominees who are insiders and serve on these committees.
3. If a director is working on a fulltime basis, he/she should not serve on the boards of more than three other publicly traded companies. If a director is not working on a fulltime basis, he/she should not serve on the boards of more than five other publicly traded companies. A vote should be cast to withhold authority from all nominees who exceed these limits.
4. If director nominees fail to attend at least 75% of their board and committee meetings a vote should be cast to withhold authority from them unless they have a valid excuse (e.g., illness).
5. If a director pledges a substantial amount of Company stock, a vote should be withheld from all nominees who allowed the pledge.
6. If the performance chart in a company’s proxy statement shows that the company has substantially and consistently underperformed its Peer Group and Broad Market Index for the past five years (a 20% underperformance will raise red flags), a vote should be cast to withhold authority from all nominees.
7. A vote to withhold authority for all board nominees should be cast when a company takes actions that are egregiously contrary to the best interests of shareholders [e.g., diminishing the ability to recruit and retain employees by reducing pension and health benefits for employees and retirees, repricing or replacement of underwater options (i.e., the shares’ fair market value has dropped below the option’s exercise price) without shareholder approval, failure to implement shareholder proposals that receive a majority vote, adoption of a package of anti-takeover devices without shareholder approval, misrepresentation of financial performance].

B. Contested Election of Board of Directors

1. By their nature, competing slates of directors must be evaluated on a case-by-case basis.
2. The factors that the agent should take into account are the personal qualifications of the nominees, the quality of the strategic plan they advance to enhance long-term corporate value, management’s historical track record, the background to the proxy contest and the equity ownership positions of individual directors.

C. Ratification of Auditors

1. Companies typically break down the fees they pay to auditors in four categories: audit, audit related, tax and other.
2. If the total of the fees for tax and other work are 20% or more of the total of the fees for audit and audit related work, a red flag is raised and serious consideration should be given to voting against the ratification of auditors.

D. Executive Compensation

1. Stock Option and Restricted Stock Plans. Such plans should be opposed if they contain any of the following elements:
    a. The plan does not specify performance standards that enable the shareholder to determine what type of performance will generate what type of award.
    b. The plan has specific performance standards but they result in excessive awards for the performance attained. This evaluation must be made on a case-by-case basis.
    c. The shares in the plan being voted on represent in excess of 5% dilution to current shareholder equity or the shares in all plans at the company represent in excess of 10% dilution to current shareholder equity. These limits can be raised on a case-by-case basis only if the company makes a specific and compelling justification for the excessive shares.
    d. The exercise price of options is not at least equal to the fair market value of the shares on the date of grant.
    e. Underwater options (i.e., the shares fair market value has dropped below the option's exercise price) can be replaced or repriced.
2. Cash Bonus Plans. Such plans should be opposed if they contain any of the following elements:
    a. The plan does not specify performance standards that enable the shareholder to determine what type of performance will generate what type of award.
    b. The plan has specific performance standards but they result in excessive awards for the performance attained. This evaluation must be made on a case-by-case basis.
3. Say on Pay. These advisory votes are complicated and should be evaluated on a case-by-case basis (except for whether such votes are held on an annual basis), weighing the following factors.
    a. The threshold query is whether a company's compensation policies and practices reflect its performance for shareholders. The agent should compare how a company has performed for shareholders compared to its peer group and also compare how a company has compensated its executives compared to
        (1) the company's peer group; and
        (2) the company's median compensation for all employees.
    b. Further queries should weigh such additional factors as:
        (1) whether restricted stock grants time vesting (a negative) or performance vesting (a positive);
        (2) the level of dilution of current shareholder equity n stock compensation plans (see section D.1.c above);
        (3) if golden parachutes are provided executives (a negative); and

(4) does the company pay tax gross-ups to its executives (a negative)?

c. There will also be an option as to whether the company should have these advisory votes on compensation on an annual basis or every two or three years. An annual basis is in the best interests of shareholders and the agent should vote that way.

4. Say on Golden Parachutes. When shareholders are asked to approve a merger/acquisition they will be given an advisory vote to approve payments made to any named executive officer in connection with the transaction. Such payments should be evaluated on a case-by-case basis, weighing the following factors.
   a. Are the executive officers losing their job because of the transaction?
      If they are not, what if any justification is there for the payment?
   b. Is the amount of payment in excess of 2.99 times the executive's average salary and bonus for the five years preceding the year in which the transaction takes place? If it is, that is a negative.
   c. Does the company pay tax gross-ups to the executive to enable the executive to escape the impact of a federal excise tax on the payments? If it does, that is a negative.

E. Employee Stock Ownership Plans

1. These are open to all fulltime and some part-time employees and provide for the purchase of stock through payroll deductions.
2. As long as these plans are in compliance with Section 423 of the Internal Revenue Code and their dilution is not excessive (see the guidelines in II.D.I.c), they should be supported.

F. Increases in Common and Preferred Stock

1. If there is a specific purpose for the increase (e.g., a stock split or acquisition of another company) and the amount sought for the increase is appropriate for the purpose (e.g., in a split where one share becomes two, a 100% increase would be appropriate, not a 200% increase), a vote should be cast in favor.
2. If the only reason being given for the increase is general corporate purposes, the increase should only be supported if the amount being sought is not more than 50% of the amount currently authorized.

G. Anti-takeover Devices

1. The practical impact of these devices is to insulate incumbent management from takeovers.
2. Takeovers can be beneficial to shareholders, since the acquirer normally is willing to pay a premium for shares. Therefore, proposals seeking the following should be opposed:
   a. Classified (staggered terms) Board
   b. Supermajority Voting Requirements
   c. Fair Price Provisions
   d. Poison Pills

   e. Eliminating the Rights of Shareholders To Act By Written Consent
   f. Eliminating the Rights of Shareholders to Call A Meeting

H. Reincorporations/Inversions From the U.S.

1. A U.S. company usually changes the state or country of its incorporation to take advantage of more favorable tax and regulatory laws in the new state or country.
2. Votes should be cast in favor of reincoporations/inversions if there are specific, legitimate business justifications in addition to clear and convincing tax benefits that will enhance the U.S. company's long-term value to shareholders and are not outweighed by the adverse impact on the company's employees and/or the local/state/federal tax base where the company currently operates.
3. Votes should be cast against reincorporations/inversions if any of the following conditions are present:
   a. There will be a significant overall dilution of management accountability and shareholder rights in the new jurisdiction, particularly if the new jurisdiction is being sought as an anti-takeover device or to limit executive or director liability.
   b. The reincorporation/inversion poses reputational risk to the U.S. company or will damage the U.S. company's governmental relationships to such a degree that it is not in the best interests of shareholders.
   c. The change to a new jurisdiction has such an adverse impact on the company's employees and/or the local/state/federal tax base where the company currently operates that it outweighs any of the business justifications for the change.

I. Mergers And Acquisitions

1. These are complicated transactions and must be decided on a case-by-case basis.
2. The agent's analysis must focus on:
   a. The strategic justifications for the transaction.
   b. The fairness of the consideration being paid and whether there is an opinion from a reputable financial advisor supporting that consideration.
   c. The fairness of any costs incurred, particularly change-in-control payments to executives.

J. Creation of Dual or Tracking Stock

1. These are complicated transactions and must be decided on a case-by-case basis.
2. The agent must scrutinize such proposals and only vote for them if the company makes a compelling justification for them.

K. Approving Other Business

1. Some companies seek shareholder approval of granting the board broad authority to take any action on such other business as may come before the meeting.
2. Such proposals should be opposed.

L. Routine Proposals

1. Such proposals do not change the structure, by laws, or operations of the company to the detriment of shareholders and they can be supported.
2. Such proposals are:
    a. Name changes.
    b. Stock splits/reverse stock splits.
    c. Indemnification and liability limitation provisions for officers and directors that conform with state law and do not affect liability for such actions as the receipt of improper personal benefits or the breach of the duty of loyalty.

III. Shareholder Proposals

A. The following types of shareholder proposals should be supported unless there are extraordinary circumstances involved:

1. Remove or submit poison pill plans (anti-takeover devices) to a shareholder vote.
2. Repeal classified (staggered terms) boards of directors.
3. Submit future golden parachutes to a shareholder voter.
4. Reduce supermajority votes.
5. Expense stock options.
6. Impose cumulative voting.
7. Separate the offices of chairman and CEO and have an independent outsider as chairman.
8. Impose confidential voting.
9. Allow shareholders access to the company's proxy materials to nominate directors if they are reasonably designed to enhance the ability of substantial shareholders to nominate directors and are not being used to promote hostile takeovers.
10. Provide for an independent "lead" director.
11. Provide that all stock plans be performance based.
12. Require that auditors only do audit and legitimate audit-related work.
13. Report on or adopt commonly accepted principles of conducts (e.g., Ceres Principles on the environment, MacBride Principles on doing business in Northern Ireland, UN International Labor Organizations Fundamental Conventions, fair lending practices, U.S. Equal Employment Opportunity Commission).
14. Disclose political contributions.
15. Majority vote standard for director elections.
16. Advisory vote on executive compensation.
17. Allow shareholders to call special meetings.

B. All other shareholder proposals shall be considered by the agent on a case-by-case basis, with reference to the foregoing specific positions on related proxy issues.