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Understanding RiskMetrics Shareholder Rights “GRId”

As we described in a [prior memo](#), RiskMetrics has replaced its Corporate Governance Quotient (CGQ) with Governance Risk Indicators (GRIDs). Using the new GRIDs methodology, RiskMetrics will identify the level of concern (low, medium and high) for each company across four categories of corporate governance metrics used by RiskMetrics: Board Structure, Compensation, Audit and Shareholder Rights. Unlike CGQ, the GRIDs metrics are both transparent – anyone can calculate a company’s scores by answering specified questions about its governance structure – and absolute – the scores are company-specific and do not depend upon practices of other companies. One of the GRIDs metrics, called “Shareholder Rights,” seeks to measure corporate takeover defenses.

The seemingly absolute nature of these measurements and scores may tend to create the impression that there is a one-size-fits-all definition of “good” governance and a consensus as to what that is. In fact, the impact on long-term shareholder value and a corporation’s economic competitiveness of various governance mechanisms is not a simple matter, analytically or legally, and, as we have previously written, directors, shareholders and other market participants should approach simple good/bad numerical metrics intended to grade public companies with caution. As with corporate governance more generally, the appropriate mix of takeover defense tools remains an area where effective director decision-making requires the deliberate exercise of company-specific discretion. No single metric or bundle of metrics can substitute for the informed business judgment of a well-advised board as to what is necessary to promote corporate and stockholder interests in dynamic, real-world circumstances. In recognition of this reality, Delaware and other law continues to recognize the authority of corporate directors to adopt and maintain defenses that a well-prepared board reasonably concludes are advisable in the circumstances facing the company.

However, given RiskMetrics’ leading position in proxy advising, boards and their advisors will likely have to spend time understanding and responding to the GRIDs. To assist in this process, we have prepared an [interactive spreadsheet](#) that any U.S. company can use to calculate its Shareholder Rights GRId score and identify the impact of particular governance changes on the GRId score. If you click on the box under the “Answer” column on our spreadsheet for any question, you will see a drop-down menu that allows you to select the particular answer for your company. The spreadsheet will then automatically recalculate the weighted raw score, the normalized score, the “Concern Level”, the graph, and the related analysis of potential actions that could be taken to increase the normalized score to a different level.

While this tool should assist in understanding and analyzing GRIDs and their operation, it bears emphasis that the Shareholder Rights GRId should be seen for what it is, a single, well-marketed, off-the-rack data-point. Good corporate governance is not a contest and cannot be reduced to a number. Companies should not weaken their ability to defend against inadequate takeover bids or other abusive tactics to increase their score on one proxy advisory firm’s calculation of “best practices.” The well-informed, well-advised board will instead continue to consider its own unique circumstances and needs in establishing governance policies and takeover defenses. The Shareholder Rights GRId may become a measurement of interest, but the essence of effective board stewardship, in the context of takeover defense as elsewhere, must remain careful and case-specific decision-making.

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