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"The Latest: Your Upcoming Proxy Disclosures"

Wednesday, January 19, 2022

Course Materials

<u>"The Latest: Your Upcoming Proxy Disclosures"</u>

Wednesday, January 19, 2022

2:00 – 3:30 pm, eastern [archive and transcript to follow]

Following up where our Fall conference left off, this critical webcast will provide you with all the latest guidance - including the latest SEC positions - about how to use your executive & director pay disclosure to improve voting outcomes and protect your board, as well as how to handle the most difficult issues on oversight, engagement and disclosure of executive & director pay.

Join these experts:

- **Mark Borges**, Principal, Compensia
- **Alan Dye**, Partner, Hogan Lovells LLP and Senior Editor, Section16.net
- **Dave Lynn**, Partner, Morrison & Foerster LLP and Senior Editor, CompensationStandards.com
- **Ron Mueller**, Partner, Gibson Dunn & Crutcher LLP

Among other topics, this program will cover:

- Say-on-Pay Trends
- Lingering Pandemic-Related Issues
- Performance-Based Compensation Disclosure
- Disclosing ESG Metrics
- Pay-Related ESG Proposals
- Clawbacks
- Director Compensation Disclosure
- CEO Pay Ratio Considerations
- Perquisites Disclosure
- Proxy Advisors
- Status of Other Dodd-Frank Rulemaking

“The Latest: Your Upcoming Proxy Disclosures”

Course Outline / Notes

1. Virtual Annual Meetings

   a) What factors should be considered in whether to hold a live or virtual annual meeting of shareholders?

   b) What trends have begun to develop with respect to the holding of a virtual annual meeting?

2. Say-on-Pay Trends

   a) To what do you attribute the higher number of failed Say-on-Pay votes in 2021? (59 failed votes exceeded only by failed votes in 2015). Is there any lesson to be learned from the high number of S&P 500 companies that failed Say-on-Pay in 2021?

   b) To what extent do you attribute the number of failed votes to companies making COVID-related changes to their executive compensation programs?

   c) What constitutes an effective response to a failed Say-on-Pay vote or a vote where there was “significant opposition” as defined by the proxy advisory firms?

   d) Also see the transcript from the December 2021 CompensationStandards.com program "Compensation Committee Responsiveness: How to Regain High Say-on-Pay Support"

3. Lingering Pandemic-Related Issues

   a) Many investors believe that companies should have returned to pre-pandemic incentive program designs in 2021 – if a company is still using a revised program due to the ongoing impacts of the COVID-related pandemic, what should it cover in its disclosure?

   b) How should a company disclose its STI plan if it used performance targets that were lower than the prior year? How much detail should the company provide of its deliberative process?

c) How should a company address its "go forward" long-term incentive compensation program if it is continuing to rely on time-based vesting and/or qualitative measures or compensation committee discretion for its LTI awards?

c) How should a company frame the disclosure of a special retention equity award or "one-time" equity award? How does a company address the issue of whether the award is a replacement for a previously-forfeited award?

d) How should a company disclose its responsiveness to shareholders if the opposition to its Say-on-Pay proposal centers on one or more COVID-related pay decisions?

4. Performance-Based Compensation Disclosure

a) How will the disclosure of performance-based compensation be affected by the more extensive disclosure that we saw in many instances in 2021?

b) In 2021, a number of companies granted extremely large, one-time equity awards to their CEO and/or other executives. What factors should a company consider in disclosing these awards? Is supplemental graphic disclosure necessary or useful?

5. Disclosing ESG Metrics

a) Should ESG-related skills and experience be added to the directors' skills matrix?

b) How should information be disclosed in the proxy statement about a company's ESG policies and practices (for example, as part of the Compensation Discussion and Analysis, or as a separate section)? Should the disclosure on human capital management mirror or summarize the information included in the Annual Report on Form 10-K?

c) Should we expect a continuing increase in the number of shareholder proposals addressing ESG issues?

d) Should a company be considering a management-driven Say-on-Climate proposal and/or disclosing it climate transition activities?

e) Should companies be considering disclosure of EEO-1 data in their proxy statements or another company-issued report?

f) Should company disclose its employee engagement activities on ESG matters?

6. Shareholder Proposals (Including Pay-Related ESG Proposals)

   a) What are likely to be the most popular shareholder proposals in 2022?

   b) Will ESG proposals lead the list?

   c) Should a company be examining its shareholder base to see what type of ESG proposals are likely to be submitted by activist/other shareholders?

   d) How should a company respond to an ESG-oriented shareholder proposal?

   e) How should a company decide whether to include an ESG metric or metrics in its short-term compensation or long-term incentive compensation program?

   f) Should a company include one or more ESG metrics in one or more of its incentive compensation plans? How should a company go about disclosing the decision to use an ESG metrics?

   g) What factors should a company evaluate when considering using an ESG metric in its executive compensation program?

7. Compensation Recovery ("Clawbacks")

   a) Discuss timing of reopening of comment period and what is likely to happen in 2022.

   b) Should the definition of an "accounting restatement" be broadened as proposed by the SEC? Would such a change make compliance with the proposed rules more challenging?

   c) Do you believe that the SEC is likely to scale back disclosure to exclude incentive awards which use stock price and/or TSR as the performance measure? If not, is the SEC likely to require companies to disclose the calculations made to determine the amount of compensation to be disgorged to the company?

   d) Should the SEC provide definitions or rely on common understandings, existing guidance and literature for terms such as "accounting restatement," "material noncompliance" and when incentive compensation is "received"?

   e) Given that most companies have adopted a compensation recovery ("clawback") policy (although most likely not nearly compliant with the proposed rule), should the SEC provide a longer transition period for companies to comply with the applicable new listing requirement?

8. Director Compensation Disclosure

   a) Has there been an increase in supplemental disclosure of the decision-making process for director compensation?

   b) Are most companies setting an annual limit on director compensation and, if so, are they highlighting this limit in their disclosure?

   c) How should a company develop a “meaningful” annual limit on director compensation?

9. CEO Pay Ratio Considerations

   a) Are companies providing supplemental disclosure when there is a significant between year-over-year CEO pay and /or median employee pay?

   b) Has CEO pay ratio had any impact on outcome of Say-on-Pay vote?

   c) Are most companies taking advantage of flexibility to use same median employee (assuming certain conditions are satisfied) or are they identifying a new median employee each year?

10. Perquisites Disclosure

   a) Did SEC C&DI on COVID-related perquisites disclosure prove useful in 2021?

   b) How are companies handling aircraft perquisite questions in current hybrid work environment?

   c) What lessons, if any, can be learned from Gulfport and ProPetro enforcement proceedings?

11. Proxy Advisory Firm Policy Updates

   a) ISS – effective for annual meetings on or after February 1, 2022

      (i) Board diversity

(A) Expanded to cover all companies (not just Russell 3000 and S&P 1500)

(B) Policy of at least one racially/ethnically diverse director takes effect in 2022

(ii) Board accountability on unequal voting rights

(A) Eliminating "grandfather" policy for companies that went public before 2015

(B) Starting in 2023, will recommend against vote for all relevant directors at companies with multi-class stock structure with unequal voting rights unless structure is reversed, removed, or subject to reasonable "sunset" provision

(C) Starting in 2022, will recommend against vote for entire board at companies with multi-class stock structure with unequal voting rights unless subject to reasonable "sunset" provision (no more than seven years)

(iii) Climate-related policies

(A) Starting in 2022, will recommend against vote for all relevant directors at companies with significant greenhouse gas emissions (starting with companies on current Climate Action 100+ Focus list) if company not taking minimum steps to assess and mitigate climate change risks to company and larger economy

(B) Will evaluate shareholder proposals seeking "Say-on-Climate" votes (either disclosure of report or approval of climate transition action plan) on case-by-case basis based on enumerated factors

(C) Will evaluate management proposals seeking shareholder approval of climate transition action plan on case-by-based basis based on enumerated factors

(iv) Change to three-year burn rate calculation methodology coming in 2023

(v) Shareholder responsiveness to Say-on-Pay vote

(A) Raising threshold for responsive analysis in Canada from 70% to 80%

(B) NOTE: U.S. policy threshold is currently 70%

b) Glass-Lewis – effective for annual meetings on or after January 1, 2022

(i) E&S metrics in incentive plans

(A) Not required, but if used, must provide robust disclosure of metrics selected, rigor of related performance targets and determination of payout opportunities; also must explain how qualitative metrics will be assessed

(ii) COVID-related program changes

(A) Still enforcing factors codified in 2021, such as justifications for significant changes in plan structure and/or lowering of performance goals; in 2022, will consider adjustments to GAAP financial results in assessing effectiveness of tying pay to performance in both STI and LTI plans

(iii) Front-loaded awards

(A) Will continue to assess multi-year awards based on quantum of award on annualized basis for full vesting period of award and overall magnitude of award on dilution of shareholder wealth

(iv) Board gender diversity

(A) Beginning in 2022, will recommend against vote for nominating committee chair at board of Russell 3000 company with more than six members unless two gender diverse directors

(B) At all other companies, require minimum of one gender diverse director

(C) Beginning in 2023,moving from fixed numerical approach to percentage-based approach: will recommend against vote for nominating committee chair at board of Russell 3000 company that is not at least 30% gender diverse

(D) Will continue to base voting recommendations on applicable state laws on gender diversity and expand guidelines to recommend in line with state laws on underrepresented community diversity

(E) Will require disclosure of diversity statistics as required by NASDAQ listing requirement by later of August 8, 2022 or date company files proxy statement for 2022 annual meeting

(F) Beginning in 2022, may recommend against vote for nominating committee chair at board of S&P 500 companies with poor disclosure of director diversity and skills; beginning in 2023, if S&P 500 company has not provided individual or aggregate racial/ethnic minority demographic information, will recommend against vote for nominating committee chair

(G) If recommend against committee chair and not up for re-election, will generally recommend against other committee member up for re-election on case-by-case basis

(v) ESG policies

(A) Will evaluate all E&S issues from standpoint of long-term shareholder value; has published policy guidelines on assessing ESG shareholder proposals

(B) Beginning in 2022, will note when Russell 1000 companies do not provide clear disclosure of board oversight of environmental and social issues; beginning in 2023, will recommend against vote for nominating committee chair at board of S&P 500 companies that fail to explicitly disclose board's role in overseeing these issues

(vi) Multi-class stock structures with unequal voting rights

(A) Beginning in 2022, will recommend against vote for governance committee chair at companies with multi-class stock structures with unequal voting rights that do not provide for reasonable "sunset" provision (seven years or less)

12. Remaining Dodd-Frank Rulemaking

a) Section 954 – Compensation recovery ("clawback") provisions

b) Section 953(a) – "Pay for performance" disclosure

c) Section 956 – Incentive-based compensation arrangements at large financial institutions

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November 18, 2021

Guidewire Software's Say-on-Pay Response

At its last annual meeting of stockholders, Guidewire Software, Inc. only received support for its named executive officer compensation from just over 57% of the votes cast on its Say-on-Pay proposal. As we know, under the policies of the major proxy advisory firms, receipt of less than 80% support (Glass Lewis) and 70% support (ISS) triggers a qualitative review (taking into consideration as variety of factors) of the following year's Compensation Discussion and Analysis for the compensation committee's responsiveness to this level of opposition. That's been a long-standing ISS policy and, as you may recall, Glass Lewis formalized its expectations in this area prior to the 2020 proxy season.

Guidewire Software filed its definitive proxy statement for its 2021 Annual Meeting of Stockholders earlier this month, and I was curious to see how the company addressed its Say-on-Pay vote and any accompanying stockholder outreach efforts. As you would expect, the company devotes a fairly significant section of it current Compensation Discussion and Analysis to describing its stockholder outreach campaign and the subsequent actions taken by the compensation committee (at page 35):

> At our December 15, 2020 annual meeting, we held a non-binding, advisory vote on the compensation of our Named Executive Officers (a "Say-on-Pay" vote), which received the support of approximately 57% of the votes cast. This was significantly lower than the support of approximately 98% of the votes cast in the previous year. To better understand this vote result and solicit stockholder feedback, we undertook a stockholder outreach campaign during fiscal year 2021 around the time of our annual stockholder meeting and again at the beginning of fiscal year 2022. We reached out to our 11 largest institutional stockholders and key investors, with aggregate holdings of approximately 54% of our outstanding shares (as of June 30, 2021), to discuss our executive compensation program and practices, solicit feedback and ensure that our Board and management have insight into the issues that are most important to our stockholders so that we can better understand our stockholders' perspectives. While not all stockholders have accepted our invitation to engage as of October 7, 2021, we have held these calls with over half of these stockholders. Our calls were led by our Chief Administrative Officer & General Counsel and our Vice President of Investors Relations, and included the Chairpersons of our Compensation Committee and Nominating and Corporate Governance Committee.
>
> During these discussions and among many viewpoints shared, our stockholders acknowledged that while the total compensation package made to our CEO, Mr. Rosenbaum, in connection with his hiring in fiscal year 2020 was significant, they generally recognized the necessity of such package to attract an executive of Mr. Rosenbaum's caliber and talent. In addition, feedback from our stockholders included that the Company and the Compensation Committee had already taken meaningful steps in fiscal year 2021 to address their concerns regarding CEO compensation levels by lowering our CEO's total compensation so that going forward, it is in line with that of an existing CEO in a comparable peer company. In general, the stockholders that we spoke with expressed support for our compensation programs in light of our cloud transition and our ESG initiatives.
>
> Some stockholders also expressed a desire for more transparent disclosure around the compensation for our Named Executive Officers, as well as continued focus on the alignment of pay for performance for our compensation arrangements. While some stockholders expressed a

preference for a reduction in stock compensation expense, others noted that they would prefer Named Executive Officers, in particular, to have and hold more equity in the Company.

As a result of these stockholder discussions and the Compensation Committee's regular annual review process, the Compensation Committee determined to take certain actions to address the stockholder concerns above. Specifically, the actions taken by the Compensation Committee included:

a. Aligning our CEO's compensation with Company performance in fiscal year 2021. As a newly hired CEO in fiscal year 2020, Mr. Rosenbaum's total compensation package was structured to be in line with that of a new CEO, taking in account his extensive experience in various senior leadership positions in the technology industry, the competitive market for similar positions at other comparable companies based on a review of compensation peer group and related survey data, and his compensation arrangements at his prior position, including compensation that he would have forfeited at his prior employer when he joined us. However, for fiscal year 2021, Mr. Rosenbaum's total compensation package was structured to be in line with that of an existing CEO, taking into account a review of our compensation peer group, the advice of Radford, as well as Mr. Rosenbaum's performance during fiscal year 2020. As a result, Mr. Rosenbaum's base salary and bonus target opportunity were not changed for fiscal year 2021 and the size of his equity grants decreased by 64%.

b. Providing more transparent disclosure regarding the compensation of our Named Executive Officers, especially that of our CEO.

c. Re-structuring our performance-based RSU program to more heavily weight long-term performance, with 50% based on company performance in fiscal year 2023, and 50% based on company performance in fiscal year 2021. Previously, the three-year performance targets constituted less than half of the long-term performance-based equity award.

d. Modifying our equity mix to eliminate TSR RSUs and replace them with performance-based RSUs based on ARR metrics, which we determined was a more appropriate metric to focus and drive our cloud transition.

e. Strengthening our corporate governance and alignment of pay with performance by increasing our stock ownership requirement for non-employee directors and executive officers;

f. Enhancing corporate governance by adopting an equity award grant policy;

g. Adding an ESG component to our bonus program for implementation in fiscal year 2022; and

h. Continuing leadership development for succession planning purposes.

We are committed to continuing our ongoing engagement with our stockholders on matters of executive compensation and corporate governance. As our stockholders' views and market practices on executive compensation evolve, the Compensation Committee will continue to evaluate and, when needed, make changes to our executive compensation program, ensuring that the program continues to reflect our pay-for-performance compensation philosophy and objectives.

As we value the opinions of our stockholders, our Board of Directors and the Compensation Committee will continue to consider the feedback received throughout the year, including when making compensation decisions for our executive officers in the future. In addition, consistent with the recommendation of our Board of Directors and the preference of our stockholders as reflected in the non-binding, advisory vote on the frequency of future Say-on-Pay votes held at our December 15, 2020 annual meeting, we intend to continue holding an annual Say-on-Pay vote.

To me, this disclosure touches all of the right points, from describing the details of the outreach campaign (including the participants on the company's side – which included directors) to providing a concise summary of the positive feedback received by, as well as the concerns shared with, the company. Of the eight actions listed by the company, I note that one item involved adding an ESG component to the annual bonus plan (which is something that many companies are considering). Although it's not completely clear, it looks as if that is being included in its fiscal 2022 annual bonus plan. It's also difficult to tell whether this decision was at the recommendation of stockholders or upon the initiative of management. But it's clearly one more instance where ESG is working its way into incentive compensation plans.

Posted by Mark Borges
Permalink: https://www.compensationstandards.com/member/blogs/compensationdisclosure/2021/11/guidewire-softwares-say-on-pay-response.html

<u>Checklist: One-Time Mega-Grant Awards – Considerations</u>

By CompensationStandards.com

There is a plethora of considerations at hand when a company's board of directors considers granting mega-grant awards. There's no strict definition to what comprises a "mega-grant," but the below are some of the defining characteristics identified by Pearl Meyer:

- Grant date value of more than 10x the executive's salary
- Represents a significant percent of common shares outstanding
- One-time multi-year award
- Extended vesting/performance horizons, often seven to ten years

Given the high-stakes nature of these mega-grant awards, we've listed out some of the key steps to take during the deliberation process.

1. **<u>Partner with External Advisors.</u>** Compensation committees may need to consider granting a one-time award due to certain circumstances, whether it be to strengthen executive retention during a particular year or prior to an IPO. Compensation committees should leverage external compensation consultants and legal advisers – benchmarking against mega-grants issued by other companies can help compensation committees during the award negotiation process. In addition, consultants can help bridge the compensation committee's goals behind the award with the executive's actions by crafting certain design features in the award. You may also want to consider tying in a clawback provision into the specific mega-grant paperwork to deter executive misconduct – this can be broader than the company's clawback policy.

2. **<u>Legal Considerations</u>**. SEC disclosure rules, as well as the company's own equity plans and policies, set the legal parameters around the mega-grant.
   - **<u>Equity Plan Limits</u>**. While many companies no longer have individual limits in their equity plans, your equity plan may have one – if so, this potential mega-grant needs to stay within those prescribed limits (and you should have some financial modeling to assess whether the limits might be crossed inadvertently due to a change in share price).
   - **<u>Proxy Disclosure</u>**. There are several areas that need to be reviewed for new/updated disclosure of a one-time equity award. One of the key areas of focus will be in the Compensation Discussion & Analysis: the purpose and

basic terms of the mega-grant, as well as a robust analysis of how the award fits into the company's compensation philosophy and existing programs, should be thoroughly disclosed in this section — take this opportunity to shape the narrative around the award.

Depending on the terms of the award, various compensation and equity tables in the proxy statement will also be impacted, including the summary compensation table, the grants of plan-based awards table and the outstanding equity awards table — the footnotes should cover the specific terms of the grant, and refer back to the CD&A for additional context.

If it's the CEO that's getting the mega-grant, you'll also need to check how it impacts the CEO pay ratio. Some companies have included a "supplemental" pay ratio excluding the CEO mega-grant. Finally (and though unlikely), consider whether the mega-grant affects the determination of named executive officers for next year's proxy statement.

- **Shareholder Approval.** Given the size of the mega-grant, you will likely need to seek shareholder approval so you don't use up the rest of the plan. However, even if your equity plan has room to spare, it may still be a good idea to go get shareholder approval — this helps tamp down on shareholder litigation risk.

3. **Accounting Needs to Be Involved**. Accounting processes and controls may need to change to appropriately account for a mega-grant. Some of the creative designs built into the awards can lead to accounting complexity — talk to the auditors early to ensure a smooth process here. In addition, if the mega-grant gets canceled later down the line or it becomes infeasible for the executive to meet the performance metrics, the company may still shoulder a larger accounting expense, so be prepared to account for those potential consequences.

4. **Investor & Proxy Advisor Expectations.** Generally, shareholders don't like mega-grants, since they will be seen as having the potential for large dilution. Similarly, proxy advisory firms (who have investors as their clientele), also don't like mega-grants. For example, in 2021, Glass Lewis noted that the most common drivers of "against" recommendations were due to excessive compensation and granting practices (including a noticeable increase in "mega-grants"). You may run the risk of ISS "against" recommendations on say-on-pay and compensation committee proposals as well, so get started on shareholder and proxy advisory firm engagement early in the proxy off-season. Finally, you should consider how the optics will play out with your employee

base and the larger public — a clear rationale and demonstration of how the award aligns with the company's goals and incentivizes better executive performance will help get more shareholder support — you'll likely need it to balance out the negative proxy advisory firm recommendations.

← NortonLifeLock's HCM Disclosure | Main | The Greenbrier's Shareholder Engagement Disclosure →

August 31, 2021

Companies Continue to Add ESG Metrics to Incentive Plans

I've been reading a lot about the upswing in companies adding (or committing to add) environmental, social and governance-related performance metrics to their incentive compensation plans. Over the past week, I've been monitoring proxy filings to see if this is really true, and it appears to be – at least at larger companies.

For example, Medtronic plc disclosed in its recently-filed definitive proxy statement that it's making changes to its fiscal 2022 annual incentive plan (largely in response to shareholder feedback) to include a "qualitative scorecard" to measure key non-financial metrics as part of its determination of bonuses under the annual Medtronic Incentive Plan (see page 44 of the Compensation Discussion and Analysis):

> In fiscal year 2021, the Committee, in consultation with the Independent Consultant modified the annual incentive plan for senior executives including NEOs to better align with Medtronic's short and long-term strategy. Beginning in fiscal year 2022, the MIP will incorporate market share as a key financial metric in addition to existing revenue growth, diluted EPS, and free cash flow metrics. The MIP will also incorporate a qualitative scorecard to measure key non-financial metrics such as quality, strategic priorities, culture and inclusion, diversity, and equity. Performance on these key non-financial metrics will be qualitatively evaluated by the committee following the close of the fiscal year. The committee believes that incorporating these quantitative and qualitative measures is critical to holistically support Medtronic's financial and strategic performance.

The same thing is happening at The Procter & Gamble Company, which notes in its latest definitive proxy statement that for purposes of its fiscal 2021-2022 annual incentive program, it's adding an "ESG Factor" to the plan's performance metrics (at page 48 of its Compensation Discussion and Analysis):

> At its August 9, 2021 meeting, the C&LD Committee elected to introduce a new Environmental, Social, and Governance (ESG) Factor that will be applied to the annual incentive (STAR) program for senior executives commencing July 1, 2021. The ESG Factor reinforces our key commitments to ESG initiatives (which the Company collectively refers to as Citizenship) by linking a portion of senior executive pay directly to outcomes and progress achieved. The C&LD Committee will determine the ESG Factor at the end of the fiscal year, based on the STAR Committee's recommendation, which is derived from an assessment of total Company fiscal year progress towards long-term Equality & Inclusion and Environmental Sustainability goals. These goals are based on various targets and ambitions reported in our annual Citizenship Report and reinforce our desire to be a "force for good and a force for growth" by ensuring a continued focus on gender diversity and multicultural representation, as well as our long-term environmental sustainability goals. The ESG Factor will adjust the Company Factor portion of the STAR award as a multiplier in the range of 80% to 120%.

As indicated, the ESG factor will act as a multiplier to the company performance factor, which is one of the two key metrics under this annual incentive plan (with a 30% overall weighting under the plan formula).

The trend also appears to be taking place in the technology sector as well. Here's what Seagate Technology Holdings plc had to say in its latest definitive proxy statement in its description of its executive compensation strategy as part of its Compensation Discussion and Analysis (at page 31):

> In July 2021, to further align our compensation philosophy with our Company values, the Compensation Committee decided to tie certain NEO compensation to the achievement of specified ESG goals. The PSUs to be granted to our NEOs in fiscal year 2022 will contain two ESG modifiers that will increase or decrease the PSU achievement level based on the Company's performance against both a social (gender diversity) goal and an environmental (greenhouse gas reduction) goal.

What's most notable to me is that Seagate is adding the ESG goals (albeit as modifiers) to its long-term incentive compensation awards. To date, most companies have been including their ESG metrics in their annual incentive plans (as is the case with Medtronic and P&G). However, I believe that it changing and that next year we will likely see a lot more LTI plans and awards that include ESG metrics as companies look for the best way to integrate these goals into their executive compensation programs.

Posted by Mark Borges
Permalink: https://www.compensationstandards.com/member/blogs/compensationdisclosure/2021/08/companies-continue-to-add-esg-metrics-to-incentive-plans.html

SIDLEY

SIDLEY UPDATE

SEC Seeks Additional Feedback on Proposed Compensation Clawback Rules

October 21, 2021

On October 14, 2021, the U.S. Securities and Exchange Commission (SEC) reopened the period to solicit input from the public on the compensation clawback rules it **proposed** in 2015 to implement Section 954 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). The proposed rules would direct the national securities exchanges to establish listing standards that would require a company to adopt, disclose and comply with a compensation clawback policy as a condition to listing securities on a national securities exchange. The proposed clawback rules were summarized in the Sidley Update available **here**.

In the **reopening release**, the SEC requests comments and supporting data on the proposed clawback rules in light of regulatory and market developments since the rules were proposed in 2015. The SEC also identifies 10 new topics on which it is specifically requesting public comment, including the following:

- The SEC asks whether it should expand the types of accounting restatements that would trigger application of a clawback policy. Under Section 954 of the Dodd-Frank Act, a clawback would be triggered "in the event that the issuer is required to prepare an accounting restatement due to the material noncompliance of the issuer with any financial reporting requirement under the securities laws." Based on its initial interpretation of the Section 954 mandate, the clawback trigger under the SEC's 2015 proposed rules was limited to material restatements of previously issued financial statements (so-called "Big R restatements"). In the reopening release, the SEC asks the public whether it should expand its interpretation and revise the rule proposal to include *all* required restatements made to correct an error in previously issued financial statements, including restatements required to correct errors that were *not* material to previously issued financial statements but would result in a material misstatement if (1) the errors were left uncorrected in the current report or (2) the error correction was recognized in the current period (so-called "Little R restatements"). This new request resulted from concerns raised that companies may not be making appropriate materiality determinations for errors to avoid triggering application of a clawback policy.
- The proposed rules contemplate that clawback policies would require the recoupment of excess incentive-based compensation received during the three-year period preceding "the date on which the issuer is required to prepare an accounting restatement," meaning the earlier to occur of (1) the date the company's board of directors, a board committee or authorized officer

(if board action is not required) concludes, *or reasonably should have concluded*, that the company's previously issued financial statements contain a material error or (2) the date a court or regulator directs the company to restate its previously issued financial statements to correct a material error. In the reopening release, the SEC asks whether it should remove the "reasonably should have concluded" standard in light of concerns that it adds uncertainty to the determination.

The chart below summarizes the highlights of the clawback rules proposed in 2015 and, where applicable, corresponding requests for comment and proposed revisions to the rule proposal the SEC raised in the reopening release. The comment period will end 30 days after the reopening release is published in the *Federal Register*.

Topic	Highlights of the 2015 Proposed Rules	2021 Requests for Comment or Proposed Revisions to the 2015 Rule Proposal
Executive Officers Covered	Any current or former executive officer, including the president, principal financial officer, principal accounting officer (or, if none, the controller), any vice-president in charge of a principal business unit, division or function, and any other person who performs policy-making functions for the company	No specific request for comment or proposed revision.
Recovery Trigger; Materiality Analysis for Errors	Accounting restatement required due to material noncompliance with any financial reporting requirement under the securities laws "Accounting restatement" was defined for purposes of the proposed rules as "the result of the process of revising previously issued financial statements to reflect the correction of one or more errors that are material to those financial statements" For purposes of the proposed rules, a restatement to correct an error that is material to previously issued financial statements shall be deemed to result from "material noncompliance" of the issuer with a financial reporting requirement under the securities laws	• Should the SEC remove the proposed definitions of "accounting restatement" and "material compliance" and instead rely on existing guidance, literature, definitions and other resources (e.g., from U.S. GAAP, IFRS and the SEC and its staff) concerning accounting errors? • Should the SEC expand the interpretation of "an accounting restatement due to material noncompliance" to include *all* required restatements made to correct an error in previously issued financial statements – not only (1) restatements that correct errors that are material to previously issued financial statements but also (2) restatements required to correct errors that were not material to previously issued financial statements but would result in a material misstatement if (a) the errors were left uncorrected in the current report or (b) the error correction was recognized in the current period? Would an alternative interpretation be preferable? • Would applying the clawback policy in the context of this additional type of restatements be challenging or unduly burdensome? Could the SEC make additional revisions to reduce the challenges or burdens, such as giving compensation committees discretion to determine whether to pursue a clawback and the amount of the recovery?

		• To what extent can the evaluation of whether an error is material be leveraged in connection with determining the need for and the amount of any clawback? Would the proposed expansion of the scope of accounting restatements that would trigger a clawback policy affect how a company conducts this evaluation and, if so, how? • Would expanding the scope cover most situations where companies may have shifted from restating previously issued financial statements to avoid triggering a clawback, or would the revised scope be over-inclusive? • How would expanding the scope affect other aspects of the proposed rules? • Is the proposed rule appropriately tailored, or would it apply too broadly to individuals and companies? • The SEC seeks data to help it evaluate the costs to companies and benefits to inve stors of revising the scope of the rule to include additional accounting restatements, particularly data that could help it quantify the number of additional clawback analyses that would be triggered.
Recovery Period	Three-year period preceding the date on which the company is required to prepare the accounting restatement, meaning the earlier to occur of (1) the date the company's board, board committee or authorized officer concludes, *or reasonably should have concluded* , that previously issued financial statements contain a material error or (2) the date a court or regulator directs the company to restate its financial statements to correct a material error	• Should the SEC remove the "reasonably should have concluded" standard in light of concerns that it adds uncertainty to the determination? Is there an alternative standard that would be less complex to apply?
"No-Fault" Recovery Mandate	Policy would apply even if an executive officer (or any other person) did not engage in misconduct and if the executive officer had no responsibility fo r the financial statement errors that required restatement	No specific request for comment or proposed revision.

Compensation Subject to Recovery	Any compensation that is granted, earned or vested based wholly or in part upon attainment of any financial reporting measure, including stock price and total shareholder return (TSR)	No specific request for comment or proposed revision.
Recoverable Amount and Potential Related Disclosures	• The amount of incentive-based compensation received by the executive officer or former executive officer that exceeds the amount of incentive-based compensation that otherwise would have been received had it been determined based on the accounting restatement • No explicit requirement to disclose how the company calculated the recoverable amount • For incentive-based compensation based on stock price or TSR, companies would be allowed to use a reasonable estimate of the effect of the accounting restatement on the applicable measure to determine the recoverable amount; where the amount of the erroneously awarded compensation is not subject to mathematical recalculation directly from the information in the accounting restatement, the proposed rules would require a company to maintain documentation of the determination of that reasonable estimate and provide such documentation to the relevant exchange	• Would investors benefit from the SEC requiring disclosure of how the company calculated the recoverable amount, including its analysis of the amount of the executive's compensation that is recoverable under the rule and/or the amount that is not subject to recovery? • For incentive-based compensation based on stock price or TSR, would investors benefit from disclosure regarding the determination and methodology that a company used to estimate the effect of stock price or TSR?
Discretion Not to Pursue Recovery	Recovery required except in two limited circumstances if the compensation committee (or majority of independent directors) determines that it would be impracticable: (1) if the direct costs of enforcing recovery would exceed the recoverable amount or (2) if recovery would violate the home country laws applicable to a foreign private issuer	No specific request for comment or proposed revision.
Failure to Comply	A company would be subject to delisting if it does not adopt, disclose and enforce its clawback policy	No specific request for comment or proposed revision.
No Indemnification or Insurance to Mitigate Losses	A company would be prohibited from indemnifying executive officers against, or paying the premiums for an insurance policy to cover, losses incurred under the clawback policy	No specific request for comment or proposed revision.

Required Clawback-Related Disclosures	• File a clawback po licy as a Form 10-K or 20-F exhibit, as applicable • In the event of a restatement, disclose in a proxy or information statement (1) the date on which the company was required to prepare each accounting restatement, the aggregate dollar amount of excess incentive-based compensation attributable to the restatement, and the aggregate dollar amount of excess incentive-based compensation that remained outstanding at the end of its last completed fiscal year; (2) the name of each individual subject to recovery from whom the company decided not to pursue recovery (including the amounts due and reason not to pursue); and (3) the name of, and amount due from, any individual with amounts of excess incentive-based compensation outstanding for more than 180 days • Clawback disclosure would have to be provided in block-text tagged format and filed as an XBRL exhibit to the proxy or information statement • Amounts recovered pursuant to a clawback policy must be deducted from the applicable column and total column of the summary compensation table and identified in a footnote to the table	• To enhance transparency, would it be useful to inve stors for the SEC to add check boxes to the cover page of the Form 10-K that indicate separately (1) whether the previously issued financial statements included in the filing include an error correction and/or (2) whether any such corrections are restatements that triggered a clawback analysis during the fiscal year? Is there an alternative method (e.g., Form 8-K) to highlight this information for investors? • Would any other disclosures be useful to investors to explain or clarify information about restatements or a company's decision as to whether or not to claw back compensation? • Would it be valuable to investors for the SEC to require that specific data points within the new clawback disclosure be separately detail tagged using Inline XBRL instead of, or in addition to, the proposed block-text tagging? If so, which disclosures and why? Should the SEC consider any tagging technologies other than XBRL?
Applicability	• All companies listed on a national securities exchange or association, including emerging growth companies, smaller reporting companies, foreign private issuers (with limited accommodations), controlled companies and companies with listed debt only • Would not apply to a listed registered management investment company if it has not awarded incentive-based compensation to any of its executive officers during the last three fiscal years	• Have there been any developments with respect to the payment of incentive-based compensation by listed registered management investment compan ies that should affect how they are treated under the proposed rules? • If an investment company or a business development company (BDC) is externally managed, should that impact how the company is treated under the proposed rules? For example, should listed or externally managed BDCs be eligible for an exemption similar to listed registered management investment companies if they do not actually pay incentive-based compensation?

		• Should the SEC reconsider any of the proposed rules' conditions or disclosure requirements with respect to investment companies?
Additional Requests for Data and Comments		• The SEC seeks specific estimates of the costs incurred by companies in implementing voluntary clawback policies to date and the costs and benefits to investors. • Would the costs and/or benefits change in implementing a clawback policy pursuant to an SEC rulemaking and the proposed expanded interpretation of "an accounting restatement due to material noncompliance"? • The SEC also requests data regarding (1) the characteristics of voluntarily adopted clawback policies (e.g., triggers, scope of executives and compensation covered) and (2) compensation structures and measures used by companies. In particular, has the voluntary adoption of clawback provisions resulted in a decrease of incentive-based compensation or an increase in compensation tied to non-financial performance by companies? • Are there any developments that should affect the SEC's consideration of the proposed rules or their potential economic effects? • Are there any changes the SEC should consider in the methodologies or estimates it used to analyze the proposed rules' economic effects in the proposing release?

Practical Implications

In light of the reopening release, companies may consider submitting or contributing to a comment letter on the proposed clawback rules or the specific requests for comment to the SEC. Interested parties may submit comments **here**, and comments received to date are available **here**.

We do not know whether the proposed rules will be adopted and, if so, when the corresponding listing standards will be proposed and become effective. It is also uncertain what the terms of the listing standards will be and whether there will be meaningful differences in the standards adopted by the major securities exchanges. In the meantime, companies may consider refreshing their compensation committees on the proposed rules and their implications and reviewing their current clawback policies for consistency with the proposed rules and analyzing what revisions would be necessary.

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November 23, 2021

Director Compensation: Pay for ESG Committee Chairs

This 29-page memo from FW Cook analyzes 2021 director pay at 300 companies of various sizes & industries. For the most part, practices around board retainers, equity grants, annual compensation limits and stock ownership guidelines have remained pretty steady from year to year. One area that is changing, though, is that more companies are establishing an ESG-related committee. Here's what FW Cook found about that:

> Thirty-six of the 300-company sample, (12%) included an Environmental, Social, and Governance (ESG)-related committee. Of those companies, 22 were in the Energy sector (61%), five were in the Financial Services sector (14%), five were in the Retail sector, and four were in the Industrial sector (11%). Additionally, 18 were large-cap (50%), 13 were mid-cap (36%), and only five (14%) were small-cap.
>
> ESG committee chair retainers were $15,000 at the median, which we observe to be aligned with the median of Nominating/Governance committee chair retainers for the 2021 study broadly. About one-third of companies with an ESG committee provide a member retainer or meeting fees.

– Liz Dunshee

Posted by Liz Dunshee
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November 22, 2021

Say-on-Pay: Pay Ratio Becoming a Voting Factor

I blogged a couple of years ago about research showing that high pay ratios might result in low say-on-pay votes. At that time, there weren't many investor policies that were expressly naming pay ratio as a factor in the say-on-pay analysis, but the data showed that investors might be signaling indirect dissatisfaction and that employees were less productive. Trillium's say-on-pay voting policy has been an exception. Lynn highlighted earlier this year that the asset manager goes above & beyond the ISS SRI voting recommendations that it typically follows – including by saying that funds will vote "against" pay if the CEO pay ratio exceeds 50:1, which is a policy that's been in place since 2019.

Now, this blog from As You Sow points out that Trillium is not alone: the pandemic and wage inequality have led more investors to incorporate "fairness" concepts into the say-on-pay analysis. That means that pay ratio caps & other fairness concepts might start to affect say-on-pay votes, especially if your shareholder base includes SRI funds, pension funds, and UK, EU and/or Canadian funds. Here are a few examples from the blog:

– Aviva, a UK asset manager with $414 billion assets under management, says in its global voting policy that "… Fairness and equality need to be more prominent principles in shaping the culture of executive pay. … Boards should also show more restraint in approving significant pay-outs or increases to pay opportunity during periods of low wage inflation, cost cutting initiatives and when there has been a loss in shareholder value." Among other problematic pay practices, Aviva expressly says that it will not support an "unjustifiable increase in the executive pay ratio relative to the median for the workforce."

– NEI Investments, a Canadian asset manager focused on responsible investing, says in its proxy voting guidelines, "A disconnect between executive compensation and salaries at lower levels of the company may de- motivate employees, and thus undermine the strategic objective of attracting and retaining talented people. Concerns have also been raised that compensation design and high pay levels for top executives do not take into account how people are actually motivated and lead to needlessly complex pay disclosure in proxy circulars." NEI votes against pay if the CEO pay ratio exceeds 3:1 or if the CEO or other NEO pay is more than 280x US median household income.

– Northstar Asset Management says in its proxy voting guidelines that it will "only approve executive compensation packages in which equity, stock options, bonuses, and benefits packages for all non-executive employees is equivalent to that of executive officers."

– Castlefield Investment Partners, another UK asset manager, says in its corporate governance & guidelines that, "Where executive base salary is in excess of between 30-35 times the UK median salary and 60-65 times that of the lowest paid employee, executive pay should be deemed excessive and remuneration should be voted AGAINST. The lower multiple should be enforced where the company in question is not a living wage employer."

– In connection with the pandemic, T. Rowe Price says in its proxy voting guidelines that, "For our 2021 proxy voting decisions, alongside our traditional assessment of pay-for-performance alignment, pay practices and absolute level of pay, we will also assess pay outcomes through the

> lens of fairness."

While these pay ratio caps are not yet widespread, it's something to watch. Long-term pay arrangements that are approved today could affect the pay ratio several years down the road – and that could be a problem for companies & directors if this trend takes off. Continued scrutiny of wage inequality as a factor in say-on-pay would mean that boards & compensation committees (and those who advise them) may need to give more weight to pay ratio as part of approving executive pay packages. You should also keep the impact of these policies in mind in connection with overseeing workforce compensation & benefits, engaging with investors, and preparing proxy disclosures.

– Liz Dunshee

Posted by Liz Dunshee
Permalink: https://www.compensationstandards.com/member/blogs/consultant/2021/11/say-on-pay-pay-ratio-becoming-a-voting-factor.html

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December 7, 2021

Visa's Perquisites Disclosure

As we now get closer to the end of the year, the proxy statement filings are really starting to lighten up. In my experience, that's fairly customary around the holidays. Still, a few significant filings are being made. Visa, for one, filed its definitive proxy statement last week and it always makes for interesting reading.

I first note the 11-page proxy summary. It contains a lot of useful information, including several pages on human capital management and other ESG topics. Most of the proxy statements I've reviewed this fall have placed their ESG discussions in the body of the proxy statement. Perhaps we'll begin to see more instances of this information being included in the proxy summary. That would certainly be consistent with the level of interest that continues to grow in this area.

But that's only the beginning on this subject. The company includes a multi-page discussion of ESG matters at the end of the Corporate Governance section of its proxy statement. What's most interesting is that the discussion doesn't just repeat what's in the Proxy Summary. The company uses this section to take a broader look at its ESG activities, including how it manages the risks and opportunities that arise from ESG issues, provides transparency of its ESG performance and enables strong management and Board oversight of its overall ESG strategy. The company also does a good job addressing the priority issues in the five areas where its focuses its ESG strategy, using a combination of narrative and graphic disclosure to report on the recent progress that it has made in each area. each informed by a materiality assessment and stakeholder engagement. It's definitely worth checking out how the company has presented this information (at page 20).

One other area that I wanted to bring to your attention is the company's discussion of its perquisites policies in the Compensation Discussion and Analysis. While Visa has always covered this topic in its CD&A, starting in 2012 it began to expand the discussion of companion travel on business related flights on its corporate aircraft. And it seems as if that disclosure has only gotten more detailed as the company has enhanced the transparency of its policies over the past decade. Here's the perquisites disclosure from the latest CD&A:

> We provide limited perquisites and other personal benefits to facilitate the performance of our NEOs' management responsibilities. For instance, we maintain a company car and driver that allows for additional security, which are used by the Chairman and Chief Executive Officer for both business and personal use, as well as some business and limited personal use by other executive officers. From time to time, our NEOs also may use the Company's tickets for sporting, cultural, or other events for personal use rather than business purposes. If an incremental cost is incurred for such use, it is included in the "All Other Compensation" column of the Summary Compensation Table for Fiscal Year 2021 if the aggregate amount paid by the Company in Fiscal Year 2021 for perquisites and personal benefits to an NEO equaled $10,000 or more.
>
> In addition, we have a policy that allows for companion travel on business-related flights on our corporate aircraft by the Chairman and Chief Executive Officer, the President, and other key employees, as approved by the Chairman and Chief Executive Officer. It is our policy that NEOs are responsible for all income taxes related to their personal usage of the Company car or corporate aircraft, as well as travel by their companions. Additionally, no NEO may use the

> corporate aircraft for exclusive personal use (not related to business) except under the terms and conditions outlined in the Company’s aircraft time-sharing agreement with the Chairman and Chief Executive Officer, or under extraordinary circumstances with the advance approval of the Chairman and Chief Executive Officer. The Compensation Committee requires that Mr. Kelly use the aircraft for all business and personal travel, based on an independent third-party finding of a bona fide security concern, which recommended that Mr. Kelly use the aircraft for all travel. Related to this requirement, Mr. Kelly is required under the terms of the aircraft time-sharing agreement to reimburse Visa for personal use of the aircraft for amounts in excess of $200,000 per fiscal year. Any personal use of the aircraft in excess of this limit by our Chairman and Chief Executive Officer pursuant to the aircraft time-sharing agreement requires him to reimburse Visa an amount (as determined by the Company) equal to the lesser of: (i) the amount that would, absent reimbursement, be reportable with respect to the Chairman and Chief Executive Officer in the Summary Compensation Table (which we refer to as the SEC Cost), or (ii) the expenses of operating such flight that may be charged pursuant to Federal Aviation Regulation Section 91.501(d) as in effect from time to time (which we refer to as the FAR Expenses). The Chairman and Chief Executive Officer’s personal use of the corporate aircraft is also subject to an annual cap of $500,000, as determined by the Company using the lesser of the SEC Cost and the FAR Expenses.

While I’ve seen a few other companies get into the details of its policies, particularly as they relate to the use of corporate aircraft, Visa’s is certainly one of the more extensive examples of this level of disclosure. Often, this information is relegated to the applicable footnote to the Summary Compensation Table, but Visa has given it a much higher profile by including it in the CD&A.

Posted by Mark Borges
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GIBSON DUNN

December 13, 2021

ISS AND GLASS LEWIS ISSUE VOTING POLICY UPDATES FOR 2022

To Our Clients and Friends:

Institutional Shareholder Services ("ISS") and Glass, Lewis & Co. ("Glass Lewis"), the two major proxy advisory firms, recently released updates to their proxy voting policies for the 2022 proxy season. The ISS U.S. policy updates are available here. The ISS updates will apply for shareholder meetings on or after February 1, 2022, except for those policies subject to a transition period. ISS plans to release an updated Frequently Asked Questions document that will include more information about its policy changes in the coming weeks.[1]

The Glass Lewis updates are included in its 2022 U.S. Policy Guidelines and the 2022 ESG Initiatives Policy Guidelines, which cover shareholder proposals. Both documents are available here. The Glass Lewis 2022 voting guidelines will apply for shareholder meetings held on or after January 1, 2022.

This alert reviews the ISS and Glass Lewis updates. Both firms have announced policy updates on the topics of board diversity, multi-class stock structures, and climate-related management and shareholder proposals. Glass Lewis also issued several policy updates that focus on nominating/governance committee chairs, as well new policies specific to special purpose acquisition companies ("SPACs").

A. Board Diversity

- *ISS – Racial/Ethnic Diversity*. At S&P 1500 and Russell 3000 companies, beginning in 2022, ISS will generally recommend "against" or "withhold" votes for the chair of the nominating/governance committee (or other directors, on a case-by-case basis) if the board "has no apparent racially or ethnically diverse members." This policy was announced last year, with a one-year transition. There is an exception for companies where there was at least one racially or ethnically diverse director at the prior annual meeting and the board makes a firm commitment to appoint at least one such director within a year.

- *ISS – Gender Diversity.* ISS announced that, beginning in 2023, it will expand its policy on gender diversity, which since 2020 has applied to S&P 1500 and Russell 3000 companies, to all other companies. Under this policy, ISS generally recommends "against" or "withhold" votes for the chair of the nominating/governance committee (or other directors, on a case-by-case basis) where there are no women on the board. The policy includes an exception analogous to the one in the voting policy on racial/ethnic diversity.

- *Glass Lewis – Gender Diversity*. Beginning in 2022, Glass Lewis will generally recommend "against" or "withhold" votes for the chair of the nominating/governance committee at Russell 3000 companies that do not have at least two gender diverse directors (as announced in connection with its 2021 policy updates), or the entire committee if there is no gender diversity on the board. In 2023, Glass Lewis will move to a percentage-based approach and issue negative voting recommendations for the nominating/governance committee chair if the board is not at least 30% gender diverse. Glass Lewis is using the term "gender diverse" in order to include individuals who identify as non-binary. Glass Lewis also updated its policies to reflect that it will recommend in accordance with mandatory board composition requirements in applicable state laws, whether they relate to gender or other forms of diversity. It will not issue negative voting recommendations for directors where applicable state laws do not mandate board composition requirements, are non-binding, or only impose reporting requirements.

- *Glass Lewis – Diversity Disclosures.* With respect to disclosure about director diversity and skills, for 2021, Glass Lewis had announced that it would begin tracking companies' diversity disclosures in four categories: (1) the percentage of racial/ethnic diversity represented on the board; (2) whether the board's definition of diversity explicitly includes gender and/or race/ethnicity; (3) whether the board has a policy requiring women and other diverse individuals to be part of the director candidate pool; and (4) board skills disclosure. For S&P 500 companies, beginning in 2022, Glass Lewis *may* recommend "against" or "withhold" votes for the chair of the nominating/governance committee if a company fails to provide any disclosure in each of these four categories. Beginning in 2023, it will generally oppose election of the committee chair at S&P 500 companies that have not provided any aggregate or individual disclosure about the racial/ethnic demographics of the board.

B. Companies with Multi-Class Stock or Other Unequal Voting Rights

- *ISS*. ISS announced that, after a one-year transition period, in 2023, it will begin issuing adverse voting recommendations with respect to directors at all U.S. companies with unequal voting rights. Stock with "unequal voting rights" includes multi-class stock structures, as well as less common practices such as maintaining classes of stock that are not entitled to vote on the same ballot items or nominees, and loyalty shares (stock with time-phased voting rights). ISS's policy since 2015 has been to recommend "against" or "withhold" votes for directors of newly-public companies that have multiple classes of stock with unequal voting rights or certain other "poor" governance provisions that are not subject to a reasonable sunset, including classified boards and supermajority voting requirements to amend the governing documents. Companies that were publicly traded before the 2015 policy change, however, were grandfathered and so were not subject to this policy. ISS had sought public comment about whether, in connection with the potential expansion of this policy to all U.S. companies, the policy should apply to all or only some nominees. The final policy does not specify, saying that the adverse voting recommendations may apply to "directors individually, committee members, or the entire board" (except new nominees, who will be evaluated case-by-case). For 2022, the current policy would continue to apply to newly-public companies. ISS tweaked the policy language to reflect that a "newly added reasonable sunset" would prevent negative voting recommendations in subsequent years. ISS considers a sunset period reasonable if it is no more than seven years.

- *Glass Lewis*. Beginning in 2022, Glass Lewis will recommend "against" or "withhold" votes for the chair of the nominating/governance committee at companies that have multi-class share structures with unequal voting rights if they are not subject to a "reasonable" sunset (generally seven years or less).

C. Climate-Related Proposals and Board Accountability at "High-Impact" Companies

- *ISS – Say on Climate*. In 2021, both shareholders and management submitted Say on Climate proposals. For 2022, ISS is adopting voting policies that document the frameworks it has developed for analyzing these proposals, as supplemented by feedback from ISS's 2021 policy development process. Under the new policies, ISS will recommend votes case-by-case on both management and shareholder proposals, taking into consideration a list of factors set forth in each policy. For management proposals asking shareholders to approve a company's climate transition action plan, ISS will focus on "the completeness and rigor of the plan," including the extent to which a company's climate-related disclosures align with Task Force on Climate-related Financial Disclosure ("TCFD") recommendations and other market standards, disclosure of the company's operational and supply chain greenhouse gas ("GHG") emissions (Scopes 1, 2 and 3), and whether the company has made a commitment to be "net zero" for operational and supply chain emissions (Scopes 1, 2 and 3) by 2050. For shareholder proposals requesting Say on Climate votes or other climate-related actions (such as a report outlining a company's GHG emissions levels and reduction targets), ISS will recommend votes case-by-case taking into account information such as the completeness and rigor of a company's climate-related disclosures and the company's actual GHG emissions performance.

- *ISS – Board Accountability on Climate at High-Impact Companies*. ISS also adopted a new policy applicable to companies that are "significant GHG emitters" through their operations or value chain. For 2022, these are companies that Climate Action 100+ has identified as disproportionately responsible for GHG emissions. During 2022, ISS will generally recommend "against" or "withhold" votes for the responsible committee chair in cases where ISS determines a company is not taking minimum steps needed to understand, assess and mitigate climate change risks to the company and the larger economy. Expectations about the minimum steps that are sufficient "will increase over time." For 2022, minimum steps are detailed disclosure of climate-related risks (such as according to the TCFD framework") and "appropriate GHG emissions reduction targets," which ISS considers "any well-defined GHG reduction targets." Targets for Scope 3 emissions are not required for 2022, but targets should cover at least a significant portion of the company's direct emissions. For 2022, ISS plans to provide additional data in its voting analyses on all Climate Action 100+ companies to assist its clients in making voting decisions and in their engagement efforts. As a result of this new policy, companies on the Climate Action 100 + list should be aware that the policy requires **both** disclosure in accordance with a recognized framework, and quantitative GHG reduction targets, and that ISS plans to address its new climate policies in its updated FAQs, so there may be more specifics about this policy when the FAQs are released.

- *Glass Lewis – Say on Climate*. Glass Lewis also added a policy on Say on Climate proposals for 2022, but takes a different approach from ISS. Glass Lewis supports robust disclosure about companies' climate change strategies. However, it has concerns with Say on Climate votes because it views the setting of long-term strategy (which it believes includes climate strategy) as the province of the board and believes shareholders may not have the information necessary to make fully informed voting decisions in this area. In evaluating management proposals asking shareholders to approve a company's climate transition plans, Glass Lewis will evaluate the "governance of the Say on Climate vote" (the board's role in setting strategy in light of the Say on Climate vote, how the board intends to interpret the results of the vote, and the company's engagement efforts with shareholders) and the quality of the plan on a case-by-case basis. Glass Lewis expects companies to clearly identify their climate plans "in a distinct and easily understandable document," which it believes should align with the TCFD framework. Glass Lewis will generally oppose shareholder proposals seeking to approve climate transition plans or to adopt a Say on Climate vote, but will take into account the request in the proposal and company-specific factors.

D. Additional ISS Updates

ISS adopted the following additional updates of note:

1. *Shareholder Proposals Seeking Racial Equity Audits*. ISS adopted a formal policy reflecting its approach to shareholder proposals asking companies to oversee an independent racial equity or civil rights audit. These proposals, which were new for 2021, are expected to return again in 2022 given the continued public focus on issues related to race and equality. ISS will recommend votes case-by-case on these proposals, taking into account several factors listed in its new policy. These factors focus on a company's processes or framework for addressing racial inequity and discrimination internally, its public statements and track record on racial justice, and whether the company's actions are aligned with market norms on civil rights and racial/ethnic diversity.

2. *Capital Authorizations*. ISS adopted what it characterizes as "minor" and "clarifying" changes to its voting policies on common and preferred stock authorizations. For both policies, ISS will apply the same dilution limits to underperforming companies, and will no longer treat companies with total shareholder returns in the bottom 10% of the U.S. market differently. ISS also clarified that problematic uses of capital that would lead to a vote "against" a proposed share increase include long-term poison pills that are not shareholder-approved, rather than just poison pills adopted in the last three years. ISS reorganized the policy on common stock authorizations to distinguish between general and specific uses of capital and to clarify the hierarchy of factors it considers in applying the policy.

3. *Three-Year Burn Rate Calculation for Equity Plans*. Beginning in 2023, ISS will move to a "Value-Adjusted Burn Rate" in analyzing equity plans. ISS believes this will more accurately measure the value of recently granted equity awards, using a methodology that more precisely measures the value of option grants and calculations that are more readily understood by the market (actual stock price for full-value awards, and the Black-Scholes value for stock options). According to ISS, when the current methodology was adopted, resource limitations

prevented it from doing the more extensive calculations needed for the Value-Adjusted Burn Rate.

4. *Updated FAQs on ISS Compensation Policies and COVID-19*. ISS also issued an updated set of FAQs (available here) with guidance on how it intends to approach COVID-related pay decisions in conducting its pay-for-performance qualitative evaluation. According to the FAQs, many investors believe that boards are now positioned to return to annual incentive program structures as they existed prior to the pandemic. Accordingly, the FAQs reflect that ISS plans to return to its pre-pandemic approach on mid-year changes to metrics, targets and measurement periods, and on company responsiveness where a say-on-pay proposal gets less than 70% support.

E. Additional Glass Lewis Updates

Glass Lewis adopted several additional updates, as outlined below. Where relevant, for purposes of comparison, the discussion also addresses how ISS approaches the issue.

1. *Waiver of Retirement or Tenure Policies*. Glass Lewis appears to be taking a stronger stance on boards that waive their retirement or tenure policies. Beginning in 2022, if the board waives a retirement age or term limit for two or more years in a row, Glass Lewis will generally recommend "against" or "withhold" votes for the nominating/governance committee chair, unless a company provides a "compelling rationale" for the waiver. By way of comparison, ISS does not have an analogous policy.

2. *Adoption of Exclusive Forum Clauses Without Shareholder Approval*. Under its existing policies, Glass Lewis generally recommends "against" or "withhold" votes for the nominating/governance committee chair at companies that adopted an exclusive forum clause during the past year without shareholder approval. With a growing number of companies adopting exclusive forum clauses that apply to claims under the Securities Act of 1933, Glass Lewis updated its policy to reflect that the policy applies to the adoption of state and/or federal exclusive forum clauses. The existing exception will remain in place for clauses that are "narrowly crafted to suit the particular circumstances" facing a company and/or include a reasonable sunset provision. By way of comparison, ISS does not have an analogous policy.

3. *Board Oversight of E&S Issues*. For S&P 500 companies, starting in 2022, Glass Lewis will generally recommend "against" or "withhold" votes for the chair of the nominating/governance committee if a company does not provide "explicit disclosure" about the board's role in overseeing environmental and social issues. This policy is taking effect after a transition year in which Glass Lewis noted concerns about disclosures it did not view as adequate. For 2022, Glass Lewis also will take the same approach for Russell 1000 companies that it took last year with S&P 500 companies, noting a concern where there is a lack of "clear disclosure" about which committees or directors are charged with oversight of E&S issues. Glass Lewis does not express a preference for a particular oversight structure, stating that boards should select the structure they believe is best for them.

4. *Independence Standard on Direct Payments for Directors*. In evaluating director independence, Glass Lewis treats a director as not independent if the director is paid to perform services for the company (other than serving on the board) and the payments exceed $50,000 or no amount is disclosed. Glass Lewis clarified that this standard also captures payments to firms where a director is the principal or majority owner. By way of comparison, ISS's independence standards likewise cover situations where a director is a partner or controlling shareholder in an entity that has business relationships with the company in excess of numerical thresholds used by ISS.

5. *Approach to Committee Chairs at Companies with Classified Boards*. A number of Glass Lewis' voting policies focus on committee chairs because it believes the chair has "primary responsibility" for a committee's actions. Currently, if Glass Lewis policies would lead to a negative voting recommendation for a committee chair, but the chair is not up for election because the board is classified, Glass Lewis notes a concern with respect to the chair in its proxy voting analysis. Beginning in 2022, this policy will change and if Glass Lewis has identified "multiple concerns," it will generally issue (on a case-by-case basis) negative voting recommendations for other committee members who are up for election.

6. *Written Consent Shareholder Proposals*. Glass Lewis documented its approach to shareholder proposals asking companies to lower the ownership threshold required for shareholders to act by written consent. It will generally recommend in favor of these proposals if a company has no special meeting right or the special meeting ownership threshold is over 15%. Glass Lewis will continue its existing policy of opposing proposals to adopt written consent if a company has a special meeting threshold of 15% or lower and "reasonable" proxy access provisions. By way of comparison, ISS generally supports proposals to adopt written consent, taking into account a variety of factors including the ownership threshold. It will recommend votes case-by-case only if a company has an "unfettered" special meeting right with a 10% ownership threshold and other "good" governance practices, including majority voting in uncontested director elections and an annually elected board.

7. *SPAC Governance*. Glass Lewis added voting guidelines that are specific to the SPAC context. When evaluating companies that have gone public through a de-SPAC transaction during the past year, it will review their governance practices to assess "whether shareholder rights are being severely restricted indefinitely" and whether restrictive provisions were submitted to an advisory vote at the meeting where shareholders voted on the de-SPAC transaction. If the board adopted certain practices prior to the transaction (such as a multi-class stock structure or a poison pill, classified board or other anti-takeover device), Glass Lewis will generally recommend "against" or "withhold" votes for all directors who served at the time the de-SPAC entity became publicly traded if the board: (a) did not also submit these provisions for a shareholder advisory vote at the meeting where the shareholders voted on the de-SPAC transaction; or (b) did not also commit to submitting the provisions for shareholder approval at the company's first annual meeting after the de-SPAC transaction; or (c) did not also provide for a reasonable sunset (three to five years for a poison pill or classified board and seven years or less for multi-class stock structures). By way of comparison, as discussed above, for several years, ISS has had voting policies that address "poor" governance provisions at newly-public

companies, including multiple classes of stock with unequal voting rights, classified boards and supermajority voting requirements to amend the governing documents. For 2022, ISS has clarified that the definition of "newly-public companies" includes SPACs.

8. *"Overboarding" and SPAC Board Seats*. Under its "overboarding" policies, Glass Lewis generally recommends "against" or "withhold" votes for directors who are public company executives if they serve on a total of more than two public company boards. It applies a higher limit of five public company boards for other directors. The 2022 policy updates clarify that where a director's only executive role is at a SPAC, the higher limit will apply.By way of comparison, ISS treats SPAC CEOs the same as other public company CEOs, on the grounds that a SPAC CEO "has a time-consuming job: to find a suitable target and consummate a transaction within a limited time period." Accordingly, SPAC CEOs are subject to the same overboarding limit ISS applies to other public company CEOs (two public company boards besides their own).

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[1] ISS also issued an updated set of FAQs on COVID-related compensation decisions.

The following Gibson Dunn lawyers assisted in the preparation of this client update: Elizabeth Ising, Ronald Mueller, and Lori Zyskowski.

Gibson Dunn's lawyers are available to assist with any questions you may have regarding these issues. To learn more about these issues, please contact the Gibson Dunn lawyer with whom you usually work in the Securities Regulation and Corporate Governance and Executive Compensation and Employee Benefits practice groups, or any of the following practice leaders and members:

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