"The Latest: Your Upcoming Proxy Disclosures"

Tuesday, January 30, 2024

Course Materials

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

Tuesday, January 30, 2024

2 to 3:30 p.m. Eastern [archive and transcript to follow]

Following up where our fall conferences left off, this critical webcast will provide you with the latest guidance on how to improve your executive and director pay disclosure — including pay versus performance disclosure and clawbacks — to improve voting outcomes and protect your board.

Hear from these experts:

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

This program will cover:

- Clawbacks
- Pay vs. Performance Disclosures
- CD&A Enhancements & Trends
- Shareholder Proposals
- Proxy Advisor & Investor Policy Updates
- Perquisites Disclosure
- ESG Metrics & Disclosures
- Say-on-Pay & Equity Plan Trends, Showing "Responsiveness" to Low Votes
- Status of Related Rulemaking

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

Course Outline/Notes

1. Clawbacks

2. Pay vs. Performance Disclosures

3. CD&A Enhancements & Trends

4. Shareholder Proposals

5. Proxy Advisor & Investor Policy Updates

6. Perquisites Disclosure

7. ESG Metrics & Disclosures

8. Say-on-Pay & Equity Plan Trends, Showing “Responsiveness” to Low Votes

9. Status of Related Rulemaking

“The Latest: Your Upcoming Proxy Disclosures”

Table of Contents — Course Materials

← SEC Rule Proposals: Human Capital & Bank Bonuses Are Still Possibilities | Main | Consider This: Corp Fin Staff's Tips for Improving PvP →

December 11, 2023

Managing a Clawback: Agenda Items for the First Special Meeting After a Restatement

This WTW memo is chock-full of helpful tips for companies that may find themselves in mandatory clawback territory. We've addressed a number of the technical and high-level questions a board will need to consider when a company faces a restatement, but this article is focused on managing a good process. For example, it lists items you should include on the agenda for your first special meeting convened after a restatement to make clawback-related process decisions. Here are two of those agenda items:

> – Determine if the clawback team is managed by external counsel using compensation experts. Fundamentally, the committee must consider conflict-of-interest questions where management helps to determine clawback values. Our view is that the risk of this being an issue for shareholders diminishes when the sums involved are smaller, the calculation is simpler, and the assumptions or judgment calls needed to complete the calculation are fewer. The more there is at stake, the more likely that both shareholders and officers will question the results and ask about the source of funds, state legal authority and individual taxation; the more complicated the process of performing the calculations becomes, the more plausible these objections will be.
>
> For these reasons, we foresee many situations where the committee would hire its own legal counsel and compensation experts to form the clawback team. To the extent it is available, preservation of attorney-client privilege in communications among the committee, the clawback team and the executive officer(s) also may be desirable.
>
> – Set forth expectations/timing for the clawback team. We anticipate the following will be deliverables from the clawback team:
>
> - A complete Compensation Review Report that details all compensation potentially impacted
> - A Calculation Methodology Report that provides details on the methodology employed and the actual calculations
> - A presentation of the potential sources of funds to satisfy the clawback
> - A recommended proxy disclosure

It also discusses how to perform clawback calculations and how the compensation committee should determine the source of clawback funds. This article is worth reading now and saving for later in the event you're involved in one of the early restatements post-effectiveness of Dodd Frank clawback policies.

– **Meredith Ervine**

Posted by Meredith Ervine
Permalink: https://www.compensationstandards.com/member/blogs/consultant/2023/12/managing-a-clawback-agenda-items-for-the-first-special-meeting-after-a-restatement.html

← Today's Webcast: "More on Clawbacks: Action Items and Implementation Considerations" | Main |
Clawback Policies Will Make Internal Investigations More Complex →

November 20, 2023

Glass Lewis: New Policies on Clawbacks & Ownership Guidelines

Late last week, Glass Lewis issued its 2024 Voting Guidelines – which include several updates on executive compensation topics. Here's an excerpt:

> – **Clawback Provisions** – In addition to meeting listing requirements, effective clawback policies should provide companies with the power to recoup incentive compensation from an executive when there is evidence of problematic decisions or actions, such as material misconduct, a material reputational failure, material risk management failure, or a material operational failure, the consequences of which have not already been reflected in incentive payments and where recovery is warranted. Such power to recoup should be provided regardless of whether the employment of the executive officer was terminated with or without cause. In these circumstances, rationale should be provided if the company determines ultimately to refrain from recouping compensation as well as disclosure of alternative measures that are instead pursued, such as the exercise of negative discretion on future payments.
>
> – **Executive Ownership Guidelines** – We have added a discussion to formally outline our approach to executive ownership guidelines. We believe that companies should facilitate an alignment between the interests of the executive leadership with those of long-term shareholders by adopting and enforcing minimum share ownership rules for their named executive officers. Companies should provide clear disclosure in the Compensation Discussion and Analysis section of the proxy statement of their executive share ownership requirements and how various outstanding equity awards are treated when determining an executive's level of ownership.
>
> In the process of determining an executive's level of share ownership, counting unearned performance-based full value awards and/or unexercised stock options is inappropriate. Companies should provide a cogent rationale should they count these awards towards shares held by an executive.
>
> – **Proposals for Equity Awards for Shareholders** – Regarding proposals seeking approval for individual equity awards, we have included new discussion of provisions that require a non-vote, or vote of abstention, from a shareholder if the shareholder is also the recipient of the proposed grant. Such provisions help to address potential conflict of interest issues and provide disinterested shareholders with more meaningful say over the proposal. The inclusion of such provisions will be viewed positively during our holistic analysis, especially when a vote from the recipient of the proposed grant would materially influence the passage of the proposal.

The updated guidelines also clarify the proxy advisor's approach to these issues:

> – **Non-GAAP to GAAP Reconciliation Disclosure** – We have expanded the discussion of our approach to the use of non-GAAP measures in incentive programs in order to emphasize the need for thorough and transparent disclosure in the proxy statement that will assist shareholders in reconciling the difference between non-GAAP results used for incentive payout determinations and reported GAAP results. Particularly in situations where significant adjustments were applied and materially impacts incentive pay outcomes, the lack of such disclosure will impact Glass

Lewis' assessment of the quality of executive pay disclosure and may be a factor in our recommendation for the say-on-pay.

– **Pay-Versus-Performance Disclosure** – We have revised our discussion of the pay-for-performance analysis to note that the pay-versus-performance disclosure mandated by the SEC may be used as part of our supplemental quantitative assessments supporting our primary pay-for-performance grade.

– **Company Responsiveness for Say-on-Pay Opposition** – For increased clarity, we amended our discussion of company responsiveness to significant levels of say-on-pay opposition to note that our calculation of opposition includes votes cast as either AGAINST and/or ABSTAIN, with opposition of 20% or higher treated as significant.

During last week's webcast for members, our expert panelists noted that these guidelines set an expectation that companies will adopt clawback policies that go beyond what's required by the listing standards adopted under the Dodd-Frank Act and SEC Rule 10D-1. That program is now available to members for on-demand listening, and the transcript will be available in a few weeks. (If you aren't already a member, you can sign up online or email sales@ccrcorp.com.)

Also check out John's blog on TheCorporateCounsel.net on Friday for info on other changes to Glass Lewis's Voting Guidelines that you'll need to know for proxy season. You may need to beef up your charters on board oversight of E&S issues….

– **Liz Dunshee**

Posted by Liz Dunshee
Permalink: https://www.compensationstandards.com/member/blogs/consultant/2023/11/glass-lewis-new-policies-on-clawbacks-ownership-guidelines.html

“Pay Versus Performance” Disclosures in the Technology and Life Sciences Sectors

As we begin to move towards the end of 2023, we have taken a closer look at the newest executive compensation disclosure item appearing in proxy statements for the first time this year – the “pay-versus-performance” table and related information. Mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act, beginning with definitive proxy statements filed for fiscal years beginning on or after December 16, 2022, reporting companies (other than foreign private issuers, registered investment companies, and emerging growth companies) are required to:

- Present in tabular form specified compensation information about their named executive officers (“NEOs”) and financial performance for their five most recently completed fiscal years (three years in the initial year of compliance);
- Provide a clear description of the relationships between each of the financial performance measures included in the required table (the “Pay-Versus-Performance” table) and the executive compensation actually paid (“CAP”) to their Chief Executive Officer (“CEO”) and, on average, their other NEOs, along with a description of the relationship between their total shareholder return (“TSR”) and their peer group’s TSR; and
- Provide a list of three to seven financial performance measures that the company determines are its most important measures used to link the CAP to its NEOs, for the most recently completed fiscal year, to company performance.

As described below, “smaller reporting companies” (“SRCs”) are eligible to comply with scaled disclosure requirements, including providing the tabular disclosure for only their three most recently completed fiscal years (two years in the initial year of compliance).

For a detailed discussion and analysis of the “pay-versus-performance” disclosure rule, please see our Thoughtful Pay Alert, *SEC Adopts New Rules for “Pay Versus Performance” Disclosure Requirement (Sept. 9, 2022).*

This Thoughtful Pay Alert summarizes our findings based on a review of the definitive and/or preliminary proxy statements filed through September 15, 2023 by over 200 technology and life sciences companies headquartered in the United States.

Companies Reviewed

We conducted an analysis of 215 technology and life sciences companies that filed their proxy statements between March 15, 2023 and September 15, 2023, as follows:

In addition, of the companies that were not SRCs, 22 companies disclosed that they did not use any financial performance measures in their short-term incentive compensation plan and granted only time-based equity awards (or only used financial performance measures that were already included in the “Pay-Versus-Performance” table). Consequently, these companies did not include a Company-Selected Measure (“CSM”) in their “Pay-Versus-Performance” table, describe the relationship between the CAP to their NEOs and a CSM, and provide a Tabular List (as discussed below), 14 of which were technology companies and eight of which were life sciences companies.

Presentation Considerations

Location of Disclosure

While the “pay-versus-performance” rule does not specify where the required disclosure should be located in the proxy statement, we found that most of the reviewed companies (52.1%) inserted the new disclosure immediately following their “CEO pay ratio” disclosure. The second most common location (20.4%) was following the required “Potential Payments Upon Termination or Change in Control” disclosure. The only other location that registered double digits was immediately following the company’s equity stock plan disclosure (the disclosure required about the number of shares available for issuance under employee stock plans both approved by shareholders and not approved by shareholders) (6.9%).

"Pay Versus Performance" Disclosures in the Technology and Life Sciences Sectors (Continued)

Location of "Pay-Versus-Performance" Disclosure

Length of Disclosure

We found that the average length of the disclosure was four pages, with the longest disclosure being 10 pages and the shortest disclosure being one page, each at one company.

Cross-Reference to Compensation Discussion and Analysis ("CD&A")

Given the nature of the pay-versus-performance disclosure – the link between pay and performance – most companies provided either a general reference to their CD&A or a cross-reference to a specific section of their CD&A where such a discussion was located for more information on how the company correlated its executive compensation to its business performance (73.0% (157 companies)), including 120 technology companies and 37 life sciences companies.

Tabular Disclosure

The required "Pay-Versus-Performance" table contains two distinct sections: information on compensation paid to a company's NEOs and information on prescribed financial performance measures – both essential to the required disclosure of the relationship between the CAP to their CEO and, on average, their other NEOs and the company's financial performance. For most companies, the most challenging aspect of preparing the "Pay-Versus-Performance" table involved the computation of the adjustments to the amounts reported for their NEOs in the Summary Compensation Table ("SCT") for each covered fiscal year, which principally involved the recalculation of the fair values of the equity awards granted or vested during each covered fiscal year as of each vesting date and outstanding at the end of each covered fiscal year as well as any equity awards granted in prior fiscal years that vested during and/or were outstanding at the end of each covered fiscal year.

Reconciliation of CAP

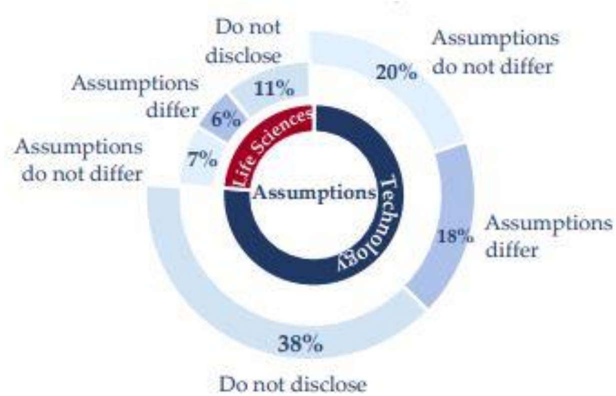
In addition to the CAP amounts reported in the "Pay-Versus-Performance" table, companies were required to include a footnote to the table providing a reconciliation between the reported SCT amounts and the CAP amounts disclosed in the table. All but four of the technology companies (154 companies) and all but one of the life sciences companies (56 companies) we reviewed provided this information using a "reconciliation table" format that, for the CEO and, on average, for the other NEOs, set out the amounts deducted from and added to the "total compensation" reported in the SCT to produce the required CAP figures.

Valuation Assumptions

If the assumptions used to recalculate the fair value of equity awards for purposes of computing CAP materially differed from those disclosed at the time of grant of such equity awards, companies were required to include a footnote to the table disclosing such assumptions. We found compliance with this requirement to be somewhat mixed among the reviewed companies. Just over one-quarter of the reviewed companies (27.4% (59 companies)), including 43 technology companies and 16 life sciences companies, expressly disclosed that the assumptions used to compute CAP did not materially differ from their grant date fair value assumptions. In view of the SEC Staff's recent interpretive guidance on the disclosure of any material changes to the valuation assumptions from those disclosed at the time of grant (see Compliance and Disclosure Interpretation Question 128D.22), it is not clear whether this conclusion was based on a review of the specific inputs used in the valuation methodology or whether a different valuation framework was used.

An additional 23.3% (50 companies), including 38 technology companies and 12 life sciences companies, disclosed that different assumptions were used to compute CAP, with 23 companies providing the updated assumptions in the footnote itself, while 12 companies simply cross-referenced the footnote in their Annual Report on Form 10-K which disclosed their equity award assumptions. Finally, a significant number of the reviewed companies (49.3% (106 companies)), including 83 technology companies and 23 life sciences companies, did not address the subject in their pay-versus-performance disclosure.

Valuation Assumptions



"Pay Versus Performance" Disclosures in the Technology and Life Sciences Sectors (Continued)

Peer Group TSR

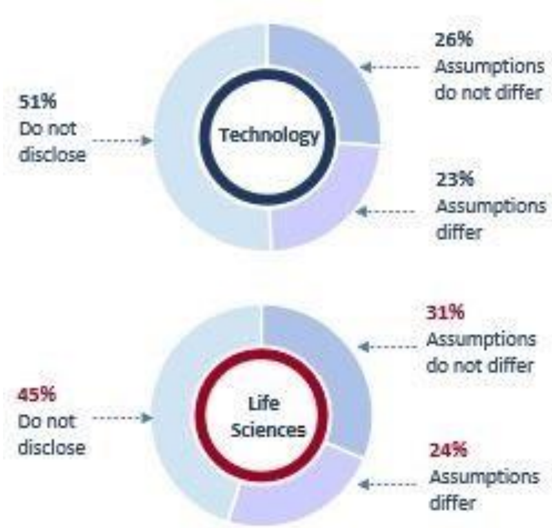
For purposes of disclosing the cumulative TSR of their peer group for each covered fiscal year, companies were permitted to use either:

- the same published industry or line-of-business index (or if an index was not used, the identity of the companies comprising the group) that they used for purposes of preparing the performance graph to be included in their Annual Report to Shareholders or, more commonly, their Annual Report on Form 10-K; or
- the companies that they used as the compensation peer group for purposes of their CD&A.

Since the "pay-versus-performance" rule requires a company that uses a group of peer companies that differs from year to year (which frequently occurs in the case of compensation peer groups) to explain the reason for the change and compare the company's cumulative TSR to that of both the newly-selected peer group and the former peer group, in our experience most companies opted to use the published industry or line-of-business index from their performance graph to satisfy this requirement.

We found that 94.5% of the companies we reviewed that were required to disclose peer group TSR (182 companies), including 75.2% of technology companies (137 companies) and 100% of life sciences companies (35 companies), chose to use a published industry or line-of-business index. Only 5.5% of the companies (all 10 of which were technology companies) used a compensation peer group. Since they were not required to do so, none of the 33 SRCs disclosed peer group TSR.

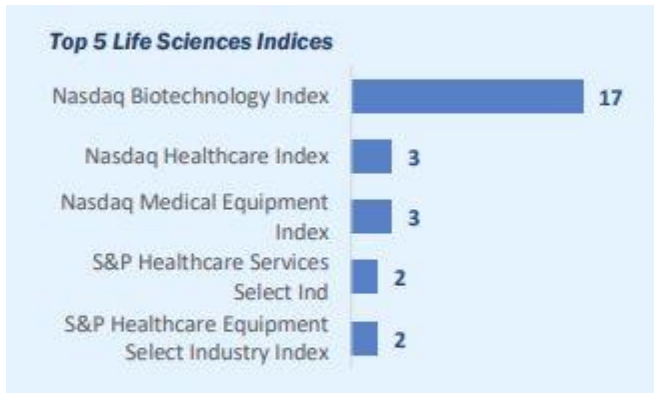
Peer Group Comparison



The most commonly used industry or line-of-business index for each sector were:

Technology Sector

Life Sciences Sector



Of the companies we reviewed, all but 11 companies that used an industry or line-of-business index used the same index as used in their performance graph. In addition, we noted that several (a total of 18) of the companies using an index appeared to use a broad equity market index, rather than the narrower published industry or line-of-business index called for under the rule.

Company-Selected Measure

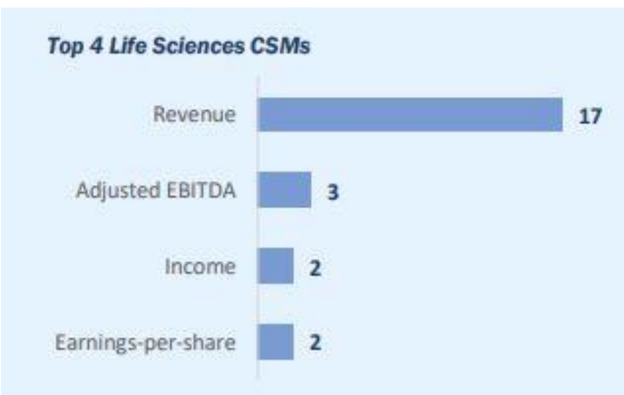
In addition to including their cumulative TSR and net income (or loss) for each covered fiscal year in the "Pay-Versus-Performance" table, companies (other than SRCs and companies that did not use any such measures in their executive compensation program) were required to select a single financial performance measure from their Tabular List (as discussed below) which, in their assessment, represented the most important financial performance measure (that was not otherwise required to be disclosed in the table) used to link the CAP to their NEOs, for the most recently completed fiscal year, to their performance.

"Pay Versus Performance" Disclosures in the Technology and Life Sciences Sectors (Continued)

The most commonly disclosed CSM's for each sector were:

Technology Sector

Life Sciences Sector



Use of Non-GAAP Performance Measure

The "pay-versus-performance" rule permits the use of non-GAAP financial performance measures as a CSM. Of the 160 companies that we reviewed which disclosed a CSM, 18.8% (30 companies), including 28 technology companies and two life sciences companies, chose a non-GAAP financial performance measure as their CSM.

"Supplemental" Performance Measure

While the "pay-versus-performance" rule permits companies to provide additional financial performance measures in their "Pay-Versus-Performance" table, we found only six companies that did so in their initial disclosure. These financial performance measures ranged from revenue (or some revenue variant, such as annual recurring revenue) to adjusted EBITDA. The others were more specialized, and included "transaction value," "adjusted contribution," and "adjusted free cash flow."

Observation: The "pay-versus-performance" rule permits a company to supplement the required disclosure with additional information (including in the "Pay-Versus-Performance" table) as long as it is not misleading and does not obscure the required information. Accordingly, it may be important for a company including an additional financial performance measure in its "Pay-Versus-Performance" table to note which of these measures is to be considered its CSM and which is the supplemental measure since the rule appears to limit companies to a single CSM. Any supplemental financial performance measures must be clearly identified as supplemental, not misleading, and not presented with greater prominence than the required disclosure. For example, depending on the facts and circumstances, a company could use a heading in the "Pay-Versus-Performance" table indicating that the disclosure is supplemental, or include language in the text of its filing stating that the disclosure is supplemental.

As previously noted above, to the extent additional financial performance measures are included in the "Pay-Versus-Performance" table, they must also be accompanied by a clear description of their relationship to the CAP to the company's NEOs. We note that each of the companies providing a supplemental financial performance measure included the measure as part of its relationship disclosure.

Relationship Disclosure

In the view of many observers, the crux of the new "pay-versus-performance" disclosure is the company's description of the relationship between each of the financial performance measures included in the "Pay-Versus-Performance" table and the CAP to their CEO and, on average, their other NEOs. This is the section of the disclosure where we saw the greatest variability in approaches to providing this information.

Form of Relationship Disclosure

The vast majority of the descriptions provided to satisfy this disclosure requirement were presented graphically – 114 companies. Of these, 89.5% were technology companies (102 companies) and 10.5% were life sciences companies (12 companies). Another 36 companies used a combination of narrative and graphical disclosure to discuss this relationship (30 technology companies and six life sciences companies). Only eight of the technology companies and two of the life sciences companies that were reviewed provided this information entirely in narrative form.

"Pay Versus Performance" Disclosures in the Technology and Life Sciences Sectors (Continued)

Observations: We noted that 74.4% of the companies (119 companies) that were required to disclosure peer group cumulative TSR "doubled up" the required relationship description of CAP and their cumulative TSR and the relationship description of their cumulative TSR and peer group cumulative TSR; using a single graphic to provide both required descriptions. In total, this included 78.2% of the technology companies (93 companies) and 21.8% of the life sciences companies (26 companies). We also noted several companies that used the same approach with their CSM – particularly where they provided a supplemental measure to the financial performance measure required in the "Pay-Versus-Performance" table.

Tabular List of Important Financial Performance Measures

Under the "pay-versus-performance" rule, reporting companies (other than SRCs and companies that did not use any financial reporting measures) were required to include a "Tabular List" of the most important financial performance measures used by the company in setting pay-for-performance compensation for the most recently completed fiscal year. This list was to include at least three, but not more than seven, financial performance measures in no particular order or rank. If a company considered only two or fewer financial performance measures when assessing pay-for-performance compensation, the company need only include in the list the measures actually considered (which may be zero). Further, in addition to the financial performance measures, a company could include non-financial performance measures (that is, operational performance measures) in the list if such measures were among its most important performance measures as long as it had disclosed its most important three (or fewer) financial performance measures.

Number of Performance Measures on Tabular List

While companies are permitted to disclose up to seven financial performance measures in their Tabular List, we found that most of the companies we reviewed 65.0% (103 companies), including 83 technology companies (80.5%) and 20 life sciences companies (19.5%), disclosed three or fewer measures, with 36 companies disclosing only one or two measures.

Companies Disclosing Non-Financial Performance Measures

Of the companies we reviewed, 21.9% (35 companies), including 26 technology companies (74.3%) and nine life sciences companies (25.7%), disclosed one or more non-financial performance measures in their Tabular List.

Observations: In our examination, we noted very few companies (in either sector) that included a list of more than five financial (and other) performance measures. Five companies disclosed six measures and one company disclosed eight. None of the companies we reviewed disclosure seven performance measures.

Most companies simply included three measures, including the CSM, or perhaps one or two additional non-financial performance measures. We saw a few companies provide explanations of the measures listed (typically where the measure might otherwise be unfamiliar to some investors), but the vast majority simply included the required list. Going forward, we believe that it may be helpful to shareholders to describe how any unusual financial measures are calculated and/or to describe the methodology used to track a non-financial performance measure (although we recognize that such information is not required).

Other Notable Disclosures

Adjusted Pension Value

In addition to recalculating the fair values of outstanding equity awards to compute CAP for purposes of the "Pay-Versus-Performance" table, if a reporting company maintained one or more defined benefit or actuarial pension plans for its NEOs, it was required to replace the aggregate change in the actuarial present value of each NEO's accumulated benefit under such plans with the sum of the service cost attributable to services rendered during each covered fiscal year and certain additional amounts if the plan was amended during a covered fiscal year. Since most technology and life sciences companies do not offer defined benefit pension plans to their employees, we only identified three companies that were required to make and disclose this adjustment when converting the total compensation amount in their SCT to CAP.

Smaller Reporting Companies

As previously noted, SRCs are subject to scaled disclosure requirements under the "pay-versus-performance" rule. Initially, SRCs need only provide a "Pay-Versus-Performance" table for the two most recently completed fiscal years (which expands to three fiscal years in 2024). In addition, SRCs were not required to account for the Adjusted Pension Value in computing CAP for their NEOs, report in the "Pay-Versus-Performance" table either peer group cumulative TSR or a CSM or include a Tabular List of important financial performance measures. Each of the SRCs we examined took full advantage of these "scaled" disclosure requirements.

Observations: Given the novelty of the new disclosure, we recommended to our clients that, if applicable, they include a statement at the beginning of their "pay-versus-performance" disclosure to indicate their SRC status, thereby explaining why their disclosure was abbreviated from that of regular filers. We also recommended comparable disclosure to our clients which did not use any financial performance measures during the last completed fiscal year to explain why they were not providing a CSM, a description of the "pay-versus-performance" relationship for that financial performance measure, or a Tabular List. These statements served to both alert investors, their advisors, and regulators as to the reason for the abbreviated disclosure.

General Observations

Of the various executive compensation disclosure rules introduced by the Dodd-Frank Act, the "pay-versus-performance" disclosure requirement is one of the most complex – both in terms of compliance and the actual information contained in the disclosure itself. While the SEC Staff resolved several of the initial compliance challenges through the issuance of Compliance and Disclosure Interpretations in February 2023 and through addition interpretations issued at the end of September, numerous questions remain as to how the required disclosure is to be prepared and presented. As a result, the initial disclosures varied significantly in terms of the detail of information that was provided and what constituted an acceptable presentation format. We anticipate that the SEC Staff, having closely reviewed the initial round of disclosures, may consider issuing further clarifications and enhancements before companies begin preparing their 2024 disclosures. In addition, the major proxy advisory firms and larger institutional shareholders may issue their own commentary on the value and utility of the new disclosure. Finally, companies may now examine the various approaches taken by their peers and other comparable companies and decide whether to make any changes to or refine their disclosure. Consequently, while the second year of compliance should be somewhat easier than this year now that companies are familiar with the intricacies of compliance, we may see noticeable enhancements in next year's disclosure as companies process this feedback and determine how best to coordinate this information with the “pay-for-performance” analyses that is an important component of their CD&As.

We also note that, as anticipated, the CAP computation turned out to be the most time-consuming aspect of the new rule. Where a company regularly granted stock options to its NEOs with monthly vesting conditions, it was often necessary to make numerous (sometimes dozens of) calculations to complete the appropriate adjustments for purposes of determining CAP. While several companies that include such stock options as part of their long-term incentive compensation programs are discussing whether to modify their option programs to move to quarterly or annual vesting, at the present time there has been no widespread movement in this direction. Nonetheless, we expect that some companies are likely to make this change and/or to continue to shift away from stock options to full value share awards (such as RSUs) if they conclude that, on balance, the advantages of shorter vesting cycles isn't sufficient to offset the compliance burden.

Need Assistance?

Compensia has extensive experience in helping companies analyze the requirements of the SEC's “pay-versus-performance” disclosure rule, as well as drafting the required disclosure. If you would like assistance in preparing your “pay-versus-performance” disclosure, or if you have any questions on the subjects addressed in this Thoughtful Disclosure Alert, please feel free to contact the authors of this Alert, Mark A. Borges at 415.462.2995 or mborges@compensia.com, Nina Jattana at 408.540.6142 or njattana@compensia.com, or Hannah Orowitz at (332) 867.0566 or horowitz@compensia.com.

November 27, 2023

Just in Time for the Holidays: More PvP CDIs Are Here!

Just before Thanksgiving, the SEC gave us even more to be thankful for — eight new and two revised CDIs on the pay-versus-performance disclosure requirements. I've paraphrased each new CDI and linked to the full text below.

1. New Question 128D.23 – Dividends or dividend equivalents paid that are not already reflected in the fair value of stock awards or included in another component of total compensation must be included in the calculation of executive compensation actually paid.

2. New Question 128D.24 – If a registrant uses more than one published industry or line-of-business index for purposes of Item 201(e)(1)(ii), the registrant may choose which index it uses for purposes of its PvP disclosure and should include a footnote disclosing the index chosen. If the registrant chooses to use a different published industry or line-of-business index from that used by it for the immediately preceding fiscal year, it is required to explain the reasons for the change in a footnote and provide a comparison against both the newly selected peer group and the peer group used in the immediately preceding fiscal year.

3. New Question 128D.25 – A registrant may not use the broad-based equity index it uses to determine the vesting of performance-based equity awards based on relative TSR as its peer group for purposes of Item 402(v)(2)(iv).

4. New Question 128D.26 – Market capitalization-based weighting is required for purposes of Item 402(v)(2)(iv) only if the registrant is not using a published industry or line-of-business index pursuant to Item 201(e)(1)(ii).

5. New Question 128D.27 – If a registrant uses a benchmarking peer group and adds or removes companies, is it required to footnote the changes and compare its cumulative total shareholder return with that of both the updated peer group and the peer group used in the immediately preceding fiscal year. However, if an entity is omitted solely because it is no longer in the business or industry or the changes were made pursuant to pre-established objective criteria, presenting both comparisons is not required, but a specific description of the change and the basis for the change must be disclosed, including the names of the companies removed. This is consistent with CDI 206.05 regarding disclosure under Item 201.

6. New Question 128D.28 – The staff will not object if a registrant that loses SRC status as of January 1, 2024 continues to include scaled disclosure under 402(v)(8) in its proxy filed not later than 120 days after its 2023 fiscal year end, forward incorporated into the 10-K. The PvP disclosure must cover fiscal years 2021, 2022, and 2023.

   Unless the registrant subsequently regains SRC status, any other proxy filed after January 1, 2024 must include non-scaled PvP disclosure. However, a registrant generally is not required to revise disclosure for prior years to conform to non-SRC status, and the staff will not object if the registrant does not add disclosure for a year prior to those included in the first filing with PvP disclosure. But the registrant should include peer TSR — measured from the market close on the last trading day before the registrant's earliest fiscal year in the table — and its numerically quantifiable performance under the Company-Selected Measure for each fiscal year in the table, and disclosure provided for all fiscal years must be XBRL tagged.

7. New Question 128D.29 – The registrant is required to include PvP disclosure in any proxy or information statement filed after it loses its EGC status, but may apply the transitional relief in Instruction 1 to Item 402(v) (that disclosure may be provided for three years instead of five in the first filing with PvP disclosure and an additional year in each of the two subsequent annual filings).

8. New Question 128D.30 – When multiple individuals served as PFO during one covered fiscal year, for purposes of calculating average compensation for the NEOs other than the PEO, the registrant may not treat the PFOs as the equivalent of one NEO. Each must be included individually in the calculation of the average, but additional disclosure regarding the impact on the calculation should be considered.

I've also included marked versions of the revised CDIs.

Revised Question 128D.07

Question: In each of 2020 and 2021, a registrant provided the same list of companies as a peer group in its Compensation Discussion & Analysis ("CD&A") under Item 402(b) but provided a different list of companies in its CD&A for 2022. With respect to a registrant providing initial Pay versus Performance disclosure in its 2023 proxy statement for three years (as permitted by Instruction 1 to Item 402(v) of Regulation S-K), may the registrant present the peer group total shareholder return for each of the three years using the 2022 peer group?

Answer: No. In this situation, the registrant should present the peer group total shareholder return for each year in the table using the peer group disclosed in its CD&A for such year. **In the 2024 proxy statement, if the registrant uses the same peer group for 2023 as it used for 2022, the registrant should present its peer group total shareholder return for each of the years in the table using the 2023 peer group. If it changes the peer group in subsequent years, it must provide disclosure of the change in accordance with Regulation S-K Item 402(v)(2)(iv).**

Revised Question 128D.18

Question: Some stock and option awards allow for accelerated vesting if the holder of such awards becomes retirement eligible. If retirement eligibility was the ~~only~~**sole** vesting condition, would this condition be considered satisfied for purposes of the Item 402(v) of Regulation S-K disclosures and calculation of executive compensation actually paid in the year that the holder becomes retirement eligible?

Answer: Yes. However, ~~for awards with additional substantive conditions, in addition to~~ **if** retirement eligibility~~, such as a market~~ **is not the sole vesting** condition ~~as described in Question 128D.16, those~~, other **substantive** conditions must also be considered in determining when an award has vested. **Such conditions would include, but not be limited to, a market condition as described in Question 128D.16 or a condition that results in vesting upon the earlier of the holder's actual retirement or the satisfaction of the requisite service period.**

– **Meredith Ervine**

Posted by Meredith Ervine
Permalink: https://www.compensationstandards.com/member/blogs/consultant/2023/11/just-in-time-for-the-holidays-more-pvp-cdis-are-here.html

July 25, 2023

SHAREHOLDER PROPOSAL DEVELOPMENTS DURING THE 2023 PROXY SEASON

To Our Clients and Friends:

This client alert provides an overview of shareholder proposals submitted to public companies during the 2023 proxy season,[1] including statistics and notable decisions from the staff (the "Staff") of the Securities and Exchange Commission (the "SEC") on no-action requests.[2]

I. SUMMARY OF TOP SHAREHOLDER PROPOSAL TAKEAWAYS FROM THE 2023 PROXY SEASON

As discussed in further detail below, based on the results of the 2023 proxy season, there are several key takeaways to consider for the coming year:

- ***Shareholder proposal submissions rose yet again.*** For the third year in a row, the number of proposals submitted increased. In 2023, the number of proposals increased by 2% to 889—the highest number of shareholder proposal submissions since 2016.

- ***The number of executive compensation proposals significantly increased, along with a continued increase in environmental and social proposals.*** Executive compensation proposals increased notably, up 108% from 2022, with the increase largely attributable to proposals seeking shareholder approval of certain executive severance agreements. The number of both environmental and social proposals also increased, up 11% and 3%

[1] **Data on No-Action Requests:** For purposes of reporting statistics regarding no-action requests, references to the 2023 proxy season refer to the period between October 1, 2022 and June 1, 2023. Data regarding no-action letter requests and responses was derived from the information available on the SEC's website.

Data on Shareholder Proposals: Unless otherwise noted, all data on shareholder proposals submitted, withdrawn, and voted on (including proponent data) is derived from Institutional Shareholder Services ("ISS") publications and the ISS shareholder proposals and voting analytics databases, with only limited additional research and supplementation from additional sources, and generally includes proposals submitted and reported in these databases for the calendar year from January 1 through June 1, 2023, for annual meetings of shareholders at Russell 3000 companies held on or before June 1, 2023. Consistent with last year, the data for proposals withdrawn and voted on includes information reported in these databases for annual meetings of shareholders held through June 1, 2023. References in this alert to proposals "submitted" include shareholder proposals publicly disclosed or evidenced as having been delivered to a company, including those that have been voted on, excluded pursuant to a no-action request, or reported as having been withdrawn by the proponent, and do not include proposals that may have been delivered to a company and subsequently withdrawn without any public disclosure. All shareholder proposal data should be considered approximate. Voting results are reported on a votes-cast basis calculated under Rule 14a-8 (votes for or against) and without regard to whether the company's voting standards take into account the impact of abstentions.

Where statistics are provided for 2022, the data is for a comparable period in 2022.

[2] Gibson, Dunn & Crutcher LLP assisted companies in submitting the shareholder proposal no-action requests discussed in this alert that are marked with an asterisk (*).

respectively, compared to 2022 and 68% and 24% respectively, compared to 2021. In contrast, governance proposals declined 14%, and civic engagement proposals declined 6%. The five most popular proposal topics in 2023, representing 43% of all shareholder proposal submissions, were (i) climate change, (ii) independent chair, (iii) nondiscrimination and diversity-related, (iv) shareholder approval of certain severance agreements, and (v) special meetings. Of the five most popular topics in 2023, all but one (shareholder approval of certain severance agreements replacing lobbying spending and political contributions) were also in the top five in 2022.

- ***While the number of no-action requests dropped significantly, the percentage of proposals excluded pursuant to a no-action request rebounded from 2022's historic low.*** Only 175 no-action requests were submitted to the Staff in 2023, representing a submission rate of 20%, down from a submission rate of 29% in 2022 and 34% in 2021. The overall success rate for no-action requests, after plummeting to only 38% in 2022, rebounded to 58% in 2023, but was still well below the 71% success rate in 2021, and marked the second lowest success rate since 2012. Success rates in 2023 improved for duplicate proposals (100% in 2023, up from 31% in 2022), procedural (80% in 2023, up from 68% in 2022), ordinary business (50% in 2023, up from 26% in 2022), and substantial implementation grounds (26% in 2023, up from with 15% in 2022), while success rates declined for resubmissions (43% in 2023, compared with 56% in 2022) and violation of law (33% in 2023, compared with 40% in 2022).

- ***The number of proposals voted on increased yet again, but overall voting support decreased significantly, and less than 3% of proposals submitted received majority support.*** In 2023, over 54% of all proposals submitted were voted on, compared with 50% of submitted proposals voted on in 2022. Despite this increase, average support for all shareholder proposals plummeted to 23.3% in 2023, down from 30.4% in 2022. The decrease in average support was primarily driven by decreased support for both social and environmental proposals, with support for social (non-environmental) proposals decreasing to 17.2% in 2023 from 23.2% in 2022 and support for environmental proposals decreasing to 21.3% in 2023 from 33.8% in 2022. And in line with lower support overall, only 25 shareholder proposals received majority support in 2023, down from 55 in 2022.

- ***More change is in store for the shareholder proposal process, as the SEC considers further amendments to Rule 14a-8, Congress homes in on reform of Rule 14a-8, and stakeholders challenge the SEC's role in the process.*** In July 2022, the SEC proposed amendments to Rule 14a-8 that, if adopted, would make it significantly more challenging for companies to exclude shareholder proposals on substantial implementation, duplication, and resubmission grounds. The SEC targeted approval of these amendments by October 2023, which means the 2024 proxy season could see further changes in how companies approach no-action requests. Additionally, the Financial Services Committee of the U.S. House of Representatives recently formed a Republican ESG Working Group, which has identified reforming the Rule 14a-8 no-action request process as a key priority of the Working Group's focus on reforming the proxy voting system for retail investors. And, as discussed below, legal action by two stakeholder groups, the National Center for Public Policy Research and the National Association of Manufacturers, could disrupt the shareholder proposal process altogether.

- ***Proponents' use of exempt solicitations grows again, and now others are joining the game.*** Exempt solicitation filings continued to proliferate, with the number of filings reaching a record high again this year and increasing almost 22% over last year and 64% compared to 2021. As in prior years, the vast majority of exempt solicitations filed in 2023 were filed by shareholder proponents on a voluntary basis—*i.e.*, outside of the intended scope of the SEC's rules—in order to draw attention and publicity to pending shareholder proposals. Interestingly, third parties have begun intervening in the shareholder proposal process by using exempt solicitation filings to provide their views on shareholder proposals submitted by unaffiliated shareholder proponents.

II. OVERVIEW OF SHAREHOLDER PROPOSAL OUTCOMES

A. Overview of Shareholder Proposals Submitted

According to the available data, shareholders submitted 889 shareholder proposals during the 2023 proxy season, up 2% from 868 in 2022—marking the third consecutive year of increased submissions and the highest number of shareholder proposal submissions since 2016. The table below shows key year-over-year submission trends across five broad categories[3] of shareholder proposals in 2023—governance, social, environmental, civic engagement, and executive compensation. As in 2022, social and environmental proposals combined represented over 50% of all proposals submitted (55% in 2023, up from 53% in 2022), with social proposals representing 33% of all proposals submitted. This was followed by governance proposals (24%),

[3] In recent years, as shareholder proposals increasingly touch on multiple topics that may overlap, the categorization of the specific subject matter of shareholder proposals has become increasingly challenging. Where a shareholder proposal addresses multiple topics, we have categorized the proposal based on what appears to be primary focus of the proposal. We categorize shareholder proposals based on subject matter as follows:

Governance proposals include proposals addressing: (i) independent board chairman; (ii) shareholder special meeting rights; (iii) proxy access; (iv) majority voting for director elections; (v) board declassification; (vi) shareholder written consent; (vii) elimination/reduction of supermajority voting; (viii) director term limits; (ix) stock ownership guidelines; and (x) shareholder approval of bylaw amendments.

Social proposals cover a wide range of issues and include proposals relating to: (i) discrimination and other diversity-related issues (including board diversity and racial equity audits); (ii) employment, employee compensation or workplace issues (including gender/ethnicity pay gap); (iii) board committees on social and environmental issues; (iv) social and environmental qualifications for director nominees; (v) disclosure of board matrices including director nominees' ideological perspectives; (vi) societal concerns, such as human rights, animal welfare, and reproductive health; and (vii) employment or workplace policies, including the use of concealment clauses, mandatory arbitration, and other employment-related contractual obligations.

Environmental proposals include proposals addressing: (i) climate change (including climate change reporting, climate lobbying, greenhouse gas emissions goals, and climate change risks); (ii) climate transition planning; (iii) plastics, recycling, or sustainable packaging; (iv) renewable energy; (v) environmental impact reports; and (vi) sustainability reporting.

Civic engagement proposals include proposals addressing: (i) political contributions disclosure; (ii) lobbying policies and practices disclosure; and (iii) charitable contributions disclosure.

Executive compensation proposals include proposals addressing: (i) severance and change of control payments; (ii) performance metrics, including the incorporation of sustainability-related goals; (iii) compensation clawback policies; (iv) equity award vesting; (v) executive compensation disclosure; (vi) limitations on executive compensation; and (vii) CEO compensation determinations.

environmental proposals (21%), civic engagement proposals (11%), executive compensation proposals (8%), and other proposals (2%).

Overview of Shareholder Proposals Submitted

Proposal Category	2023	2022	2023 vs 2022[4]	Observations
Social	297	287	↑3%	The largest subcategory, representing 25% of all social proposals, continued to be nondiscrimination and diversity-related proposals, with 76 submitted in 2023 (though down from 97 submitted in 2022 and 128 in 2021). Of note, 22 proposals related to reproductive healthcare were submitted in 2023, up from only four such proposals submitted in 2022.
Governance	212	246	↓14%	Independent board chair proposals were the most common governance proposal, representing 40% of all governance proposals with 85 submitted (up from 20% in 2022). Proposals related to shareholder special meeting rights represented 20% of governance proposals (down from 46% in 2022).
Environmental	188	169	↑11%	The largest subcategory, representing 80% of these proposals, continued to be climate change proposals, with 150 submitted in 2023 (increasing from 129 in 2022 and 83 in 2021). Of note, there were 37 climate change proposals submitted in 2023 that specifically addressed issues related to climate transition planning.
Civic engagement	97	103	↓6%	Lobbying spending proposals decreased to 34 in 2023 from 45 in 2022, and political contribution proposals decreased to 30 in 2023 from 45 in 2022. New types of civic engagement proposals this season included 12 proposals from an ESG-skeptic perspective focused on the company's political speech or affiliations with certain entities.
Executive compensation	75	36	↑108%	The largest subcategory of executive compensation proposals continued to be those requesting boards seek shareholder approval of certain severance agreements, representing 63% of these proposals, up from 44% in 2022. There were seven proposals requesting that companies include, or report on the possibility of including, social- or environmental-focused performance measures in executive compensation programs (such as greenhouse gas ("GHG") emissions and maternal morbidity) up from just two such proposals submitted in 2022 (but down from 15 proposals submitted in 2021).

[4] Data in this column refers to the percentage increase or decrease in shareholder proposals submitted in 2023 as compared to the number of such proposals submitted in 2022.

The table below shows that four of the five most common proposal topics during the 2023 proxy season were the same as those in the 2022 proxy season, with proposals requesting boards seek shareholder approval of certain severance agreements joining the top five in 2023 and lobbying spending and political contributions proposals leaving the top five. A significant decrease in the number of special meeting proposals drove down the concentration of the top five proposal topics, which collectively represented 45% of all shareholder proposals submitted in 2023, down from 49% in 2022.

Top Shareholder Proposals Submitted to Public Companies

2023	2022
Climate change (17%)	Climate change (15%)
Independent chair (10%)	Special meetings (13%)
Nondiscrimination & diversity (9%)	Nondiscrimination & diversity (11%)
Shareholder approval of severance agreements (5%)	Independent chair (5%)
Special meetings (5%)	Lobbying spending (5%) Political contributions (5%)

B. Overview of Shareholder Proposal Outcomes

As shown in the table below, the 2023 proxy season saw both new and continued trends in proposal outcomes that emerged in the 2022 proxy season: (i) the percentage of proposals voted on increased moderately from 2022 (54% in 2023 compared to 50% in 2022), but overall support declined by over seven percentage points (23.3% in 2023 compared to 30.4% in 2022); (ii) the percentage of proposals excluded through a no-action request increased slightly in 2023 (9% in 2023 compared to 8% in 2022); and (iii) the percentage of proposals withdrawn decreased significantly to 16% in 2023 compared to 26% in 2022.

Social and environmental proposals both continued to see decreased withdrawal rates in 2023, with 20% of social proposals withdrawn (compared to 30% in 2022) and 32% of environmental proposals withdrawn (compared to 51% in 2022). These significant drops in withdrawal rates may reflect, among other factors, the impact of Staff Legal Bulletin No. 14L (Nov. 3, 2021) ("SLB 14L") on the viability of no-action requests in 2022, leading shareholders to demand more robust commitments from companies in exchange for withdrawal. The percentage of withdrawn governance proposals (4%) dropped (down from 9% in 2022, but almost level with 5% in 2021), reflecting the fact that certain individuals, who are the main proponents of many governance proposals, generally are disinclined to withdraw their proposals, even when a company has substantially implemented the request.

Shareholder Proposal Outcomes[5]	2023[6]	2022[7]
Total number of proposals submitted	889	868
Excluded pursuant to a no-action request	9% (82)	8% (71)
Withdrawn by the proponent	16% (143)	26% (224)
Voted on	54% (483)	50% (438)

Voting results. Shareholder proposals voted on during the 2023 proxy season averaged support of 23.3%, down significantly from 30.4% in 2022. Notably, looking at just environmental proposals, average support decreased significantly to 21.3%, compared to 33.3% support in 2022. Consistent with the trend we saw in 2022 and as discussed below, the lower support for climate change proposals appears to be driven by an increase in more prescriptive proposals which have received lower support from institutional investors. Similarly, support for social (non-environmental) proposals decreased to 17.2% in 2023 from 23.2% in 2022, likely for the same reason. Average support for governance proposals decreased to 31.1% from 36.7% in 2022. Of particular note, 62 of the 483 proposals that were voted on during the 2023 proxy season received less than 5% shareholder support, the lowest resubmission threshold under Rule 14a-8(i)(12)—up from 47 proposals that received less than 5% support in 2022 and consistent with the overall decline in shareholder support.

Four of the top five shareholder proposals by average shareholder support in 2023 were different from those reported in 2022. As in prior years, corporate governance proposals received generally high levels of support. The table below shows the five shareholder proposal topics voted on at least three times that received the highest average support in 2023.

Top Five Shareholder Proposals by Voting Results[8]

Proposal	2023	2022[9]
Simple majority vote (eliminate supermajority voting)	57.9% (13)	84.1% (6)
Report on climate lobbying	38.2% (8)	N/A
Freedom of association	36.4% (6)	N/A
Majority voting for director elections	35.7% (3)	N/A
Workplace health and safety audit	34.0% (4)	N/A

5 Excludes proposals that, for other reasons, were reported in the ISS database as having been submitted but that were not in the proxy or were not voted on, including, for example, due to a proposal being withdrawn but not publicized as such or the failure of the proponent to present the proposal at the meeting. As a result, in each year, percentages may not add up to 100%.

6 As of June 1, 2023, ISS reported that 118 proposals (representing 13% of the proposals submitted during the 2023 proxy season) remained pending.

7 As of June 1, 2022, ISS reported that 108 proposals (representing 12% of the proposals submitted during the 2022 proxy season) remained pending.

8 The numbers in the parentheticals indicate the number of times these proposals were voted on.

9 In 2022, the five shareholder proposals voted on at least three times that received the highest average support included board declassification, eliminate/reduce supermajority voting, submit severance agreement to shareholder vote, report on civil rights/racial equity audit, and majority voting for director elections.

Majority-supported proposals. As of June 1, 2023, only 25 proposals (less than 3% of the 889 proposals submitted) received majority support, as compared with 55 proposals (or 6% of the 868 proposals submitted in 2022) that had received majority support as of June 1, 2022. Notably, after several consecutive years of growth in the number of majority-supported climate change proposals, only two climate change proposals received majority support in 2023, including one proposal that the company supported. This is in contrast to nine majority-supported climate change proposals in each of 2022 and 2021, and four in 2020. Despite the sharp decline in majority-supported proposals in 2023, there were a few noteworthy proposals that received majority support, including a proposal requesting the commission of a third-party assessment of the company's commitment to freedom of association and collective bargaining rights[10] and two human capital management proposals—the first requesting a report on the effectiveness of the company's diversity, equity and inclusion ("DEI") efforts and metrics[11] and the second requesting a report on the company's efforts to prevent workplace harassment and discrimination.[12]

Governance proposals accounted for 64% of proposals that received majority support in 2023 (compared with 38% in 2022). While governance proposals have consistently ranked among the highest number of majority-supported proposals, the steep decline in the number of climate-related shareholder proposals receiving majority support resulted in a much narrower range of majority-supported proposals than in recent years. Environmental and social proposals together represented 24% of majority-supported proposals, while 8% of majority-supported proposals related to executive compensation, each of which related to requesting that boards seek shareholder approval of certain severance agreements. As of June 1, 2023, only one civic engagement proposal received majority support. The table below shows the proposals that received majority support.

Proposals that Received Majority Support

Proposal	2023	2022[13]
Simple majority vote (eliminate supermajority voting)	8	6
Shareholder special meeting rights	5	9
Climate change	2	9
Shareholder approval of severance agreements	2	4
Majority voting in director elections	1	2
Lobbying spending	1	2
Permit shareholder action by written consent	1	1
Workplace health and safety audit	1	0
Majority of votes cast to remove directors	1	0
Report on effectiveness of DEI efforts and metrics	1	0
Report on prevention of workplace harassment and discrimination	1	0
Third-party report on freedom of association and collective bargaining rights	1	0

[10] *See* Starbucks Corporation's proxy statement at 81, *available* here.

[11] *See* Expeditors International of Washington, Inc's proxy statement at 40, *available* here.

[12] *See* Wells Fargo & Company's proxy statement at 115, *available* here.

[13] Indicates the number of similar proposals that received majority support in 2022.

III. Shareholder Proposal No-Action Requests

A. *Overview of No-Action Requests*

Submission and withdrawal rates. The number of shareholder proposals challenged in no-action requests submitted to the Staff during the 2023 proxy season again decreased significantly, down 28% compared to 2022 and down 35% compared to 2021, likely reflecting lower success rates in 2022.[14]

No-Action Request Statistics

	2023	**2022**	**2021**
No-action requests submitted	175	244	272
Submission rate[15]	20%	29%	34%
No-action requests withdrawn	33 (19%)	56 (23%)	64 (24%)
Pending no-action requests (as of June 1)	0	3	4
Staff Responses[16]	142	185	204
Exclusions granted	82 (58%)	71 (38%)	144 (71%)
Exclusions denied	60 (42%)	114 (62%)	60 (29%)

Most common arguments. The below table, reflecting the number of no-action requests that contained each type of argument, reveals a change in the most-argued grounds for exclusion from ordinary business in 2022 to procedural in 2023. As in recent years, ordinary business and substantial implementation continued to be the most argued substantive grounds for exclusion.

Most Common Arguments for Exclusion

	2023	**2022**	**2021**
Procedural	71 (41%)	64 (26%)	86 (32%)
Ordinary Business	68 (39%)	106 (43%)	96 (35%)
Substantial Implementation	38 (22%)	91 (37%)	114 (42%)
False/Misleading	17 (10%)	42 (17%)	38 (14%)

Success rates. This year, the Staff granted approximately 58% of no-action requests, a significant increase over the 38% success rate in 2022, though still significantly below the 71% success rate in 2021 and the 70% success rate in 2020. Consistent with 2022, the Staff most often granted no-action requests based on procedural (representing 48% of successful requests), ordinary business (representing 34% of successful requests), and substantial implementation (representing 9% of successful requests) grounds. Notably, no-action requests based on these three grounds together accounted for over 90% of successful requests in 2023 compared to 77%

14 Gibson Dunn remains a market leader for handling shareholder proposals and no-action requests during proxy season, having filed approximately 20% of all shareholder proposal no-action requests each proxy season for several years.

15 Submission rates are calculated by dividing the number of no-action requests submitted to the Staff by the total number of proposals reported to have been submitted to companies.

16 Percentages of exclusions granted and denied are calculated by dividing the number of exclusions granted and the number denied, each by the number of Staff responses.

of successful requests in 2022, evidencing a narrower concentration of the grounds on which successful requests were granted. While the success rate for substantial implementation arguments for environmental proposals increased to 20% (up from 6% in 2022), only one such request was actually successful,[17] and the increase is instead attributable to there being a smaller number of total requests for exclusion on substantial implementation grounds. No social proposals were successfully excluded on substantial implementation grounds, a continuation of the downward trend noted in 2022, where 3% of social proposals were successfully excluded on substantial implementation grounds. Meanwhile, the high success rate for proposals seeking exclusion on duplicate proposal grounds was driven by the overall decrease in no-action requests seeking exclusion on this basis—in 2023 only eight no-action requests sought exclusion on duplicate proposal grounds,[18] down from 23 in 2022.

Success Rates by Exclusion Ground[19]

	2023	2022	2021
Duplicate proposals	100%	31%	38%
Procedural	80%	68%	84%
Ordinary business	50%	26%	65%
Resubmissions	43%	56%	100%
Violation of law	33%	40%	50%
Substantial implementation	26%	15%	67%

Top proposals challenged. This year, the most common proposals for which companies submitted no-action requests (on both procedural and substantive grounds) were those requesting a policy requiring an independent board chair, amendments to the company's governing documents to expand and/or lower the threshold for special meetings, a policy requiring the board to seek shareholder approval of certain executive severance arrangements, and audits related to racial equity or civil rights issues.

The no-action requests related to independent board chair proposals made the following arguments: procedural (7), duplicate proposal (2), vague or false/misleading (1), substantial implementation (1), and resubmission (1). The successful requests were granted on the following grounds: procedural (4), duplicate proposal (2), substantial implementation (1), and resubmission (1).

The no-action requests related to special meeting proposals made the following arguments: procedural (6), vague or false/misleading (3), violation of law (2), absence of power/authority (1), and substantial implementation (1). Two of the successful requests were granted on procedural grounds, and one was granted on substantial implementation grounds. The no-action requests related to shareholder approval of certain executive severance agreements made the

17 *Alliant Energy Corp.* (avail. Mar. 30, 2023).

18 Of the eight no-action requests that sought exclusion on duplicate proposal grounds, four no-action requests were granted on the basis of duplicate proposals, one no-action request was withdrawn and three no-action requests were granted on alternative grounds without the Staff issuing a decision on the duplicate proposal argument.

19 Success rates are calculated by dividing the number of no-action requests granted on a particular ground by the total number of no-action requests granted or denied on that ground, excluding no-action requests that are withdrawn or granted on an alternative ground.

following arguments: procedural (8), ordinary business (1), and substantial implementation (1). Seven of the successful requests were granted on procedural grounds, and one was granted on ordinary business grounds. The no-action requests related to racial equity and civil rights audits made the following arguments: procedural (6), resubmission (2), and substantial implementation (1). The two successful requests were both granted on procedural grounds.

	Submitted	Denied	Granted	Withdrawn
Independent board chair	11	2 (18%)	8 (73%)	1 (9%)
Special meeting right/threshold	10	5 (50%)	3 (30%)	2 (20%)
Shareholder approval of certain executive severance agreements	10	2 (20%)	8 (80%)	N/A
Racial equity/civil rights audit	9	4 (44%)	2 (22%)	3 (33%)

B. Key No-Action Request Developments

There were a number of noteworthy procedural and substantive developments in no-action decisions this year.

1. Success Rates Rose, but Submissions Declined

This season saw a rebound in the success rates of no-action requests, with the Staff granting relief to approximately 58% of no-action requests, a significant increase over the 38% success rate in 2022, but still well below the 71% success rate in 2021. This rise in success rates can be attributed in part to a decline in overall no-action requests submitted (175 in 2023, compared to 244 in 2022), with companies being more reluctant to challenge proposals given last year's low success rate. This decrease in submissions was driven in part by a marked decrease in submission of no-action requests related to environmental (21 in 2023, compared to 38 in 2022) and social (61 in 2023, compared to 92 in 2022) proposals.

The overall decline in submissions was also driven in part by companies declining to submit no-action requests arguing for exclusion on substantive bases that appear to be increasingly disfavored by the Staff. For example, during this season no proposals were successfully excluded under three key substantive bases—Rule 14a-8(i)(1), which permits the exclusion of proposals that are improper under state law; Rule 14a-8(i)(3), which permits exclusion if the proposal or supporting statement is false or misleading or otherwise in violation of proxy roles; and Rule 14a-8(i)(6), which permits the exclusion of proposals where the company would lack the power or authority to implement the proposal. Similarly, there were only three no-action requests submitted this season that argued for exclusion under the economic relevance exclusion in Rule 14a-8(i)(5) and none were successful. The Staff under Chair Clayton sought to revitalize the economic relevance exclusion in 2017 through the issuance of Staff Legal Bulletin No. 14I (Nov. 1, 2017), but that guidance was subsequently rescinded by SLB 14L. Finally, the number of no-action requests arguing for exclusion on the basis of substantial implementation under Rule 14a-8(i)(10) dropped dramatically in 2023 (only 38 in 2023, compared to 91 in 2022). While the success rate for substantial implementation rebounded modestly from 2022 (26% in 2023, compared to 15% in 2022), it continued to be well below recent years.

2. Continued Implications of SLB 14L on No-Action Requests

As discussed in our 2022 client alert,[20] in November 2021, the Staff issued SLB 14L,[21] which rescinded certain Staff guidance and reversed prior no-action decisions, upending the Staff's recent approach to the application of the economic relevance exclusion in Rule 14a-8(i)(5) and the ordinary business and micromanagement exclusions in Rule 14a-8(i)(7). SLB 14L rejected a more recent company-specific approach to significance and expressed the Staff's current view that the analytical focus should be on whether the proposal raises issues with a broad societal impact such that they transcend the company's ordinary business and whether the proposal raises issues of broad social or ethical concern when interpreting economic relevance. Moreover, SLB 14L rejected the Staff's long-standing position requiring a sufficient nexus between a proposal and the social concern raised in the proposal.[22] SLB 14L also changed the Staff's approach on assessing micromanagement, focusing on the granularity sought by a proposal and the extent to which a proposal limits company or board discretion rather than the prior focus on whether a proposal included requests for specific detail, timeframes, or targets.

The position taken by the Staff in SLB 14L appears to have led to an overall decline during the 2022 and 2023 seasons in the number of no-action requests arguing ordinary business grounds under Rule 14a-8(i)(5) and Rule 14a-8(i)(7). For the second year in a row, no proposals were excluded during the 2023 season under Rule 14a-8(i)(5). The 2023 season saw a continued decline in the number of no-action requests arguing ordinary business grounds under Rule 14a-8(i)(7), likely due to SLB 14L. In total, 58 no-action requests, or 6.5% of all proposals, challenged proposals on ordinary business grounds in 2023 (excluding those making only a micromanagement argument), with a success rate of 45%. By comparison, 95 no-action requests, or 11% of all proposals, challenged proposals on ordinary business grounds in 2022 (excluding those making only a micromanagement argument), with a success rate of 26%, and 87 no-action requests challenged proposals on ordinary business grounds in 2021, with a success rate of 64%. This drastic change in success rates for ordinary business arguments between 2021 and 2022 was likely the result of the Staff's abandonment of the traditional company-specific approach to significance. Instead, under SLB 14L, the Staff is focused on whether a proposal raises issues with a broad societal impact, without regard to any connection between those issues and a company's business operations. Moreover, the Staff has demonstrated increased willingness to recognize more topics as transcending ordinary business.

The number of shareholder proposals excluded on ordinary business grounds rebounded from the historically low success rate in 2022. Notably, the increase in success rates appears to be attributable in part to the fact that some proponents, apparently emboldened by their success in 2022 and the Staff's unwillingness to grant exclusion on the grounds of ordinary business, submitted proposals that addressed matters that have traditionally been viewed as clearly relating to ordinary business. It remains to be seen whether the Staff has recalibrated its evaluation of ordinary business arguments and whether proponents will return to submitting only those types

[20] *Available here.*

[21] *Available here.*

[22] *See* SLB 14H (Oct. 22, 2015) at n.32 ("Whether the significant policy exception applies depends, in part, on the connection between the significant policy issue and the company's business operations.") *citing* SLB 14E (Oct. 27, 2009) (stating that a proposal generally will not be excludable "as long as a sufficient nexus exists between the nature of the proposal and the company")).

of proposals that the Staff has refused to exclude since SLB 14L.

3. Resurrection of Micromanagement

SLB 14L impacted the Staff's approach on assessing micromanagement during the 2022 season: companies submitted 45 no-action requests arguing for exclusion on micromanagement grounds, and the Staff only granted two of those requests on that basis, representing a success rate of 8%. In contrast, the 2023 season saw a significant increase in the success of no-action requests on micromanagement grounds, with companies submitting 41 no-action requests arguing for exclusion on micromanagement grounds as at least one basis for exclusion, and the Staff granting eight of those requests on that basis, representing a success rate of 31%.[23] The rise in the success rate of micromanagement arguments is partially attributable to the fact that proponents are increasingly drafting more prescriptive proposals. Successfully excluded proposals spanned different categories of proposals, including those related to GHG emissions and climate change, death benefits for senior executives, corporate charitable contributions and pilot participation in a program to mitigate risks of forced labor in a company's supply chain.

4. Effects of 14a-8 Amendments on No-Action Requests

As discussed in our 2022 client alert, in September 2020, the SEC adopted amendments (the "Amended Rules") to key aspects of the SEC's shareholder proposal rule. The 2023 proxy season was only the second season following the application of the Amended Rules.

Among other changes, the Amended Rules increased the resubmission thresholds in Rule 14a-8(i)(12), which permits exclusion of a proposal if a similar proposal was last included in the proxy materials within the preceding three years and if the last time it was included it received: less than 5% support, if proposed once within the last five years (increased from 3%); less than 15% support, if proposed twice within the last five years (increased from 6%); or less than 25% support, if proposed three or more times within the last five years (increased from 10%). During the 2023 proxy season, only three proposals were successfully excluded under Rule 14a-8(i)(12) for failure to receive a sufficient level of support,[24] compared to five such successful exclusions in 2022 and one such successful exclusion in 2021. Notably, however, none of the three proposals excluded under Rule 14a-8(i)(12) in 2023 would have been excluded under the lower resubmission thresholds of the prior rules.

The Amended Rules also require each proponent to affirmatively state that the proponent is available to meet with the company, either in person or via teleconference, between 10 and 30 calendar days after the submission of the shareholder proposal, and each proponent must provide the company with contact information, as well as specific business days and times that the

[23] As noted above, success rates are calculated by dividing the number of no-action requests granted on a particular ground by the total number of no-action requests granted or denied on that ground.

[24] *Chevron Corp. (Unitarian Universalist Association)* (avail. Apr. 4, 2023)* (concurring with exclusion under Rule 14a-8(i)(12)(ii) where the similar proposal last received 12.38% of the votes cast, less than the 15% required); *CVS Health Corp. (Steiner)* (avail. Mar. 28, 2023) (concurring with exclusion under Rule 14a-8(i)(12)(iii) where the similar proposal last received 21.53% of the votes cast, less than the 25% required); *PNC Financial Services Group, Inc.* (avail. Feb. 28, 2023) (concurring with exclusion under Rule 14a-8(i)(12)(iii) where the similar proposal last received 7.69% of the votes cast, less than the 15% required).

proponent is available to meet with the company to discuss the proposal. In eight instances this season, compared to three instances in 2022, the Staff concurred with the exclusion of proposals where proponents did not provide such a statement of engagement availability. Notably, in two instances, as discussed below, the Staff also noted that the "[p]roponent has not provided sufficient proof of email delivery," and in one instance, the Staff noted that the proponent had not demonstrated, "solely by providing its asset manager's contact information, that it is 'apparent and self-evident' that the asset manager has authority to engage with the [c]ompany for purposes of Rule 14a-8(b)(1)(iii)."[25]

5. Noteworthy Procedural Challenges

This season saw the Staff address numerous procedural challenges. Notable challenges include:

- *Sufficient proof of email delivery must be provided.* As noted above, in two instances this season, companies challenged proposals under Rule 14a-8(f) where a proponent's representative did not provide a statement of engagement availability, as required under Rule 14a-8(b)(1)(iii).[26] In both instances, the company timely notified the representative of the deficiency, but received no response curing the defect. Immediately after the submission of both no-action requests, the representative sent to each company and the Staff photographs of emails that were purportedly timely sent, without forwarding the purported emails. The Staff granted exclusion in both instances, noting that the "[p]roponent has not provided sufficient proof of email delivery" and referencing SLB 14L, which provides that "[i]f a shareholder uses email to respond to a company's deficiency notice, the burden is on the shareholder or representative to use an appropriate email address (e.g., an email address provided by the company, or the email address of the counsel who sent the deficiency notice), and we encourage them to seek confirmation of receipt."

- *Procedural exclusion may be granted in unique instances, despite deficient company notices.* In one instance this season,[27] the Staff granted the exclusion of a proposal under Rule 14a-8(f) where the proponent failed to establish the requisite eligibility to submit the proposal as required under Rule 14a-8(b)(1)(i), while at the same time criticizing the company's deficiency notice notifying the proponent of the defect. The proposal, which was received by the company via FedEx, only contained the P.O. box address of the proponent's trust and no other contact information. The company mailed a timely deficiency notice to the proponent at the P.O. box address provided and received no response curing the deficiency. Following the submission of the no-action request seeking exclusion, the proponent alerted both the company and the Staff that he had not included other contact information in his submission materials for security purposes and did not regularly check the P.O. box address included in the materials, and, as a result, missed the deficiency notice sent by the company. The Staff granted exclusion of the proposal, noting that although "the [c]ompany's Rule 14a-8(f) notice was deficient in numerous respects, the [c]ompany did notify the [p]roponent of the problem – using the only method of contact that the [p]roponent provided." The Staff found that because the

[25] *Chevron Corp. (Meyer Memorial Trust (S))* (avail. Apr. 4, 2023)*.

[26] *Textron Inc.* (avail. Jan. 23, 2023)*; *The Allstate Corp.* (avail. Jan. 23, 2023).

[27] *Yum! Brands, Inc.* (avail. Mar. 31, 2023).

proponent did not check the singular method of contact provided until *after* the deadline for responding to the deficiency notice, the proponent's failure to remedy the defect "could not have been caused by the inaccuracy and incompleteness of the deficiency notice."

- *Manner of deficiency notice delivery matters.* In one instance this season, the Staff indicated in its response to the company's no-action request that it was unable to concur with exclusion of a proposal because the Staff claimed it was unable to determine if the proponent had timely received the company's deficiency notice because of the manner in which the company sent the deficiency notice. The deficiency notice was sent via overnight delivery to the proponent at a multi-unit complex, no signature was obtained upon delivery, and the company did not send a copy by email to the proponent.

- *Specificity in the wording of deficiency notices.* In one instance this season, while the Staff found that a proponent's submission was deficient under Rule 14a-8(b)(1)(iii) because it did not contain the proponent's contact information, the Staff denied relief and criticized the company's deficiency notice, stating that "rather than focusing on the defect, the [c]ompany's deficiency notice asserted that the Rule 14a-8(b)(1)(iii) statement already provided was wholly inadequate because it came from the [p]roponent's representative instead of from the [p]roponent." The Staff also noted that a proponent's representative may send this information on behalf of a proponent.

6. Third Party Attempts to Intervene in No-Action Request Process

While stakeholder activism has historically focused on the submission of shareholder proposals, the past several years have demonstrated the increasing politicization of the shareholder proposal process. And the 2023 proxy season marked a notable development in the evolution of stakeholder activism in this process—in at least one instance this season, a third party sought to intervene in the consideration by the Staff of a pending no-action request. The third party, which had no known relationship to the shareholder proponent that submitted the proposal, sent the Staff a response to the no-action request arguing against exclusion of the proposal. In its response to the third party's letter, the company argued that allowing third parties to intervene in the no-action process is inconsistent with Rule 14a-8, would increase the administrative burdens on companies and shareholder proponents as well as place additional pressure on the Staff's resources, would encourage submissions by a multitude of third parties whose interests may not be aligned with those of shareholders (or even the shareholder proponent), and would inappropriately turn the no-action request process into a forum for public policy debates. The Staff ultimately concurred with the exclusion of the proposal for reasons unrelated to the attempted third-party intervention and did not include the third party's correspondence in the file posted on the SEC website with the company's no-action request.

IV. Key Shareholder Proposal Topics During the 2023 Proxy Season

A. Human Capital and Social Proposals

Proposals focused on nondiscrimination and diversity constituted the largest subcategory (representing 26%) of social proposals submitted in 2023. These proposals were largely focused on racial equity and civil rights, DEI efforts, and gender and racial pay equity. While many social proposals in 2023 were tied to race and equality issues, proposals focused on reproductive rights and human rights assessments gained momentum. The 2023 proxy season also saw a significant rise in social proposals directly challenging the traditional ESG consensus. These ESG-skeptic social proposals included proposals requesting that companies, among other things, roll back plans to undertake a racial equity audit, conduct a cost/benefit analysis of DEI programs, conduct a racial equity and "return to merit" audit, and report on risks of supporting reproductive rights.

1. Racial Equity/Civil Rights Audit and Nondiscrimination Proposals

In 2023, there were 55 shareholder proposals that addressed issues of racial equity and civil rights, including workplace discrimination, audits of workplace practices and policies, and related topics, compared to 51 similar proposals submitted in 2022 and 38 in 2021.

The most frequent type of these proposals were 32 proposals calling for a racial equity or civil rights audit analyzing each company's impacts on the "civil rights of company stakeholders" or "civil rights, diversity, equity, and inclusion." Similar to prior years, these proposals often included the required or optional use of a third party to conduct the audit, with input to be solicited from employees, customers, civil rights organizations, and other stakeholders. These proposals were primarily submitted by the Service Employees International Union, with other filers including the New York State Comptroller (on behalf of the New York State Common Retirement Fund), Trillium Asset Management, and As You Sow. Fourteen of these proposals went to a vote, with ISS generally recommending votes "against" the proposal and average support of 22.4%, down from 21 such proposals that went to a vote in 2022, with average support of 45.3%. Four companies unsuccessfully sought to exclude a racial equity/civil rights audit proposal, arguing for exclusion on ordinary business, resubmission, substantial implementation, violation of law, vagueness or false/misleading, or procedural grounds.

The remaining 23 proposals related to workplace nondiscrimination, including requests to report on the prevention of workplace harassment and discrimination, eliminating discrimination through inclusive hiring, and requests to commission a non-discrimination audit analyzing the impacts of the company's DEI policies on "civil rights, non-discrimination, and return to merit." Of these, 13 proposals, including each of the "return to merit" proposals, were ESG-skeptic proposals submitted by the National Center for Public Policy Research ("NCPPR") and The Bahnsen Family Trust, with supporting statements that focused on concerns about discrimination against "non-diverse" employees or discrimination based on religious and political views. Five companies sought to exclude workplace nondiscrimination proposals, three of which were successful on procedural grounds.[28] The 12 proposals that went to a vote averaged 10.3% support, with ESG-skeptic social proposals garnering an average of only 1.5% support.

[28] *CVS Health Corp. (Baker)* (avail. Mar. 28, 2023); *The Coca-Cola Co.* (avail. Feb. 21, 2023); *Deere & Co.* (avail. Dec. 5, 2022).

2. Diversity, Equity, and Inclusion Efforts and Metrics

The number of proposals requesting disclosure of DEI data or metrics or reporting on the effectiveness of DEI efforts or programs remained relatively flat, with 35 such proposals submitted in 2023 and 34 submitted in 2022, up from 21 comparable proposals submitted in 2021. Of these, 25 proposals were withdrawn or otherwise not included in the proxy statement and five went to a vote with average support of 29.3%. One proposal received majority support, with 57.3% of votes cast in favor, at Expeditors International of Washington, Inc. Three companies sought exclusion of DEI proposals via no-action request, two of which were withdrawn and one of which was unsuccessful. As in 2022 and 2021, As You Sow was the main driver behind these proposals, submitting or co-filing 27 DEI proposals, 21 of which were withdrawn. Other filers included the New York State Comptroller on behalf of the New York State Common Retirement Fund (submitting two proposals), Amalgamated Bank (submitting three proposals co-filed by As You Sow), and Myra Young (submitting four proposals, three of which were co-filed by As You Sow).

3. Gender/Racial Pay Gap

The number of shareholder proposals calling for a report on the size of a company's gender and racial pay gap and policies and goals to reduce that gap increased during the 2023 proxy season. In 2023, shareholders submitted 16 proposals (up from nine proposals submitted in 2022), including two resubmissions to companies that received pay gap proposals last year. Six gender/racial pay gap proposals were submitted by Arjuna Capital and 10 were submitted by James McRitchie and/or Myra Young. Average support for these proposals decreased in 2023 as compared to 2022: the nine proposals voted on in 2023 received average support of 31.7% (with none receiving majority support), a significant decrease from average support of 42.6% for the five proposals voted on in 2022 (with two receiving majority support). Six proposals were not included in the company's proxy statement, with one proposal withdrawn after the company agreed to disclose quantitative median and statistically adjusted pay gaps. Each of these proposals targeted unadjusted pay gaps. In addition, where the company did not already provide adjusted wage gap information for comparable jobs (*i.e.*, what women and ethnic minorities are paid compared to their most directly comparable male and nonminority peers, adjusted for seniority, geography, and other factors), the proposals requested that the company also provide adjusted pay gap disclosure.

4. Reproductive Rights

In the wake of the overturn of *Roe v. Wade*, a focus area for the 2023 proxy season involved shareholder proposals requesting a report on the effect of reproductive healthcare legislation, including risks from state policies imposing restrictions on reproductive rights (including impacts on employee hiring, retention, and productivity) or on risks related to fulfilling information requests for enforcement of laws criminalizing abortion access. One ESG-skeptic proposal was submitted, requesting a report on risks and costs associated with opposing or altering company policy in response to state policies regulating abortion, with the supporting statement focusing on concerns that the company took a "pro-abortion stance" by opposing pro-life legislation and offering employees health coverage for travel costs. The number of reproductive rights proposals increased this season, with 22 such proposals submitted in 2023, up from four comparable proposals submitted in 2022, including three resubmissions to companies that received these proposals last year. The main proponents were Arjuna Capital, Tara Health

Foundation, and Change Finance P.B.C. Five companies sought to exclude these proposals, arguing for exclusion on ordinary business, micromanagement, and/or procedural grounds, but three requests were unsuccessful and the remaining two requests were withdrawn. Average support for these proposals decreased in 2023 as compared to 2022: the 11 proposals voted on in 2023 received average support of 10.8% (with none receiving majority support), a significant decrease from average support of 22.3% for the two proposals voted on in 2022.

5. Human Rights

The number of shareholder proposals relating to human rights, including those calling for a report on or an impact assessment of risks of doing business in countries with significant human rights concerns or for an assessment of the human rights impacts of certain products or operations, increased during the 2023 proxy season. In 2023, shareholders submitted 37 human rights proposals (up from 16 proposals submitted in 2022), including seven to companies that received human rights proposals last year. Fourteen of these proposals were ESG-skeptic proposals submitted primarily by the National Legal and Policy Center ("NLPC") and NCPPR, generally requesting reports on the risk of the company's operations in China. The 24 human rights proposals voted on received average support of 12.3% overall, with the proposals focused on operations in China receiving average support of 4.9% and the remainder receiving average support of 19.6%. Five companies sought to exclude these proposals via no-action requests, but only one was successful on resubmission grounds; two that argued for exclusion on ordinary business, micromanagement, and vagueness or false/misleading grounds were unsuccessful, and the remaining two were withdrawn.

B. Continued Focus on Climate Change and Environmental Proposals

As was the case in 2022, climate change-related proposals were the largest group of environmental shareholder proposals in 2023 by a large margin, representing 80% of all environmental proposals (and 17% of all proposals) submitted. There were 150 climate change-related proposals submitted in 2023, up from 130 proposals submitted in 2022 and 83 proposals submitted in 2021. This season also saw an increase in the number of environmental and climate change proposals excluded via no-action requests, with 13 excluded during the 2023 season (five were excluded on procedural grounds, one was excluded on substantial implementation grounds, and seven were excluded on ordinary business or micromanagement grounds), and five were excluded during the 2022 season (four were excluded on procedural grounds and one was excluded on substantial implementation grounds). Consistent with the overall rise in the success of ordinary business arguments more generally (as described in Part III above), the rise in environmental and climate change proposals excluded via no-action request can be at least partially attributed to the fact that some proponents have drafted more prescriptive proposals. In 2023, three environmental proposals were excluded as relating to the company's ordinary business matters, all of which requested that healthcare companies serve plant-based food options in their hospitals,[29] and four climate change proposals were excluded on

[29] *UnitedHealth Group Inc.* (avail. Mar. 16, 2023); *Elevance Health, Inc. (Beyond Investing LLC)* (avail. Mar. 6, 2023)*; *HCA Healthcare, Inc. (Beyond Investing LLC)* (avail. Mar. 6, 2023).

micromanagement grounds, two seeking detailed information on asset retirement obligations[30] and two seeking implementation of specific accounting methods.[31]

Climate change proposals took various forms, including requesting adoption of GHG emissions reduction targets (usually in alignment with net zero scenarios), disclosure of climate transition plans, disclosures regarding climate-related lobbying, changes to investments in and underwriting policies relating to fossil fuel production projects, and disclosures of risks related to climate change. Of these, the most common were proposals focusing on GHG emissions reductions targets and climate transition plans. Other popular climate change proposals included 17 proposals related to climate lobbying aligned with the Paris Agreement, nine proposals that requested the company phase out underwriting and lending for new fossil fuel exploration and development projects, and six proposals related to stranded carbon assets and asset retirement obligations due to energy companies' decommissioning of refineries. As with social proposals, there was also a rise in climate change proposals from the ESG-skeptic perspective, including proposals calling for a board committee to analyze risks of committing to decarbonization, reports on the feasibility of achieving the company's net zero targets, and requests to "rescind" a prior shareholder proposal requesting adoption of Scope 3 emissions reduction targets.

Continuing the trend from 2022, while the number of climate change proposals submitted and voted on increased significantly in 2023 compared to prior years, the average support for these proposals, the number receiving majority support and the withdrawal rates of these proposals are all at their lowest rates in at least three years. Similarly, ISS support for climate change proposals in 2023 decreased significantly, with ISS recommending votes "for" 47% of climate change proposals, down from 61% in 2022. This dramatic shift is likely largely due to the rise of more prescriptive proposals that went to a vote. As opposed to proposals seeking disclosure of company policies and practices related to climate change, these proposals related to specific business decisions that the company should undertake. For example, proposals focused on barring financial and insurance companies from underwriting or lending for new fossil fuel development received average support of 7.2%. By contrast, less prescriptive proposals seeking disclosure of companies' climate transition plans received average support of 26.9%.

[30] *Phillips 66* (avail. Mar. 20, 2023)*; *Valero Energy Corp.* (avail. Mar. 20, 2023).

[31] *Amazon.com, Inc.* (avail. Apr. 7, 2023, *recon. denied* Apr. 20, 2023)* (seeking measurement and disclosure of specific activities encompassed in the company's Scope 3 GHG emissions reporting); *Chubb Limited (Green Century Equity Fund)* (avail. Mar. 27, 2023) (seeking the phase out of underwriting risks associated with new fossil fuel exploration and development projects as a method for aligning the company's activities with limiting global temperature rise to 1.5 degrees Celsius).

Climate Change Proposal Statistics: 2023 vs. 2022			
	2023	**2022**	**2023 vs. 2022**
Submitted	150	130	↑16%
Voted on	70	41	↑73%
Average support	22.0%	33.4%	↓35%
Majority support	2	9	↓78%
Withdrawn (as percentage of submitted)	30%	52%	↓42%

1. Climate Transition Plans

There were 37 shareholder proposals submitted that related to issuing a climate transition report disclosing the company's GHG emissions reduction targets as well as policies, strategies, and progress made toward achieving those targets. These proposals usually called for long-term GHG emissions targets that cover Scopes 1, 2, and 3 emissions and that are in alignment with a 1.5 degree Celsius net zero scenario and the Science Based Targets initiative, including by asking companies to expand established emissions targets that do not meet these requirements. The supporting statements of these proposals frequently referenced concerns that disclosure of emissions reduction targets is not enough to address climate risk or provide sufficient accountability for achieving those targets and that investors would benefit from increased disclosure regarding the company's strategies to achieve those targets, including relevant timelines and metrics against which to measure progress. Five climate transition plan proposals focused on the impact of the company's climate transition strategy on relevant stakeholders under the International Labour Organization's "just transition" guidelines. Four climate transition proposals targeted financial institutions and called for transition plans to align the company's financing activities with its GHG emissions reduction targets, citing each company's membership in the Net Zero Banking Alliance. The primary proponents of these proposals were As You Sow (submitting 19 proposals), Green Century Capital Management (submitting five proposals), and Mercy Investment Services (submitting three proposals). Most of these proposals (a total of 25) were withdrawn or otherwise not included in the company's proxy statement, with 12 going to a vote, of which nine were voted on as of June 1, 2023, receiving average support of 28.7%.

2. Continued Focus on GHG Emissions

There were 52 proposals submitted related to measuring GHG emissions or adoption of GHG emissions reduction targets, typically in alignment with the Paris Agreement and often time-bound and covering all three scopes of emissions. Two of these proposals requested that the company recalculate its GHG emissions baseline to exclude emissions from material divestitures, both of which went to a vote (one after an unsuccessful no-action request arguing for exclusion on multiple proposals grounds), receiving average support of 18.4%. Two GHG emissions proposals were submitted by ESG-skeptic shareholder proponents, with one calling for the company to "rescind" a shareholder proposal to reduce Scope 3 GHG emissions that received majority support in 2021 and another requesting a report on the company's progress toward and feasibility of achieving net zero emissions by 2025 with a supporting statement that focused on obstacles to achieving net zero and expressed concerns that the company's net zero targets equate to "a false and misleading promise." Six companies sought to exclude GHG emissions proposals via no-action request, arguing for exclusion on ordinary business, micromanagement, multiple proposals, and substantial implementation grounds. Two requests were successful, one on procedural grounds and one that involved a proposal that requested that the company "measure and disclose scope 3 GHG emissions from its full value chain" and defined that to include scope 3 emissions of certain customers. The company argued that the proposal sought to micromanage the company by dictating the methodology and scope of activities included in the company's Scope 3 emissions reporting, thus limiting management's discretion in this regard.[32] A majority of the emissions-focused proposals (28) were voted on, receiving average support of 24.8%.

3. Other Environmental Proposals

Other popular environmental proposals (not related to climate change) predominantly focused on plastic pollution and sustainable packaging (totaling 14 of the 38 non-climate environmental proposals submitted in 2023), deforestation in supply chains (eight proposals), and other sustainability practices. Five non-climate environmental proposals were excluded via no-action requests: two on procedural grounds, and three on ordinary business grounds (which, as described above, all related to serving plant-based food options in the company's hospitals). Of the remaining proposals, 17 were withdrawn or otherwise not included in the company's proxy statement and 11 were voted on (and averaged 17.3% support). Of the 11 proposals voted on so far, six related to plastic use, plastic pollution, or sustainable packaging materials; one related to environmental and health impacts of the company's operations; one related to deforestation; one related to supply chain water risks; one related to impacts of oil spills; and one related to plant-based milk pricing. None of the proposals received majority support, and the highest level of support received were proposals relating to the use of plastics, which received between 25.3% and 36.9% support.

C. A New Governance Topic: Advance Notice Bylaws

A new focus area for the 2023 proxy season involved 28 shareholder proposals requesting that the company amend its bylaws to require shareholder approval for certain advance notice bylaw amendments, including timing of nominations, disclosure requirements for director nominees, and disclosure of nominating shareholders' affiliates. These proposals were in response to the adoption of changes made by companies to the advance notice provisions in their bylaws following the SEC's adoption of new universal proxy card rules in November 2021, which became effective in August 2022.[33] In support of these proposals, shareholder proponents expressed concern that certain bylaw amendments would make it burdensome for shareholders to nominate directors. All 28 of these proposals were submitted by John Chevedden's associates, primarily James McRitchie. Five no-action requests were submitted on this topic, and all were withdrawn. Nine of these proposals were withdrawn or otherwise not included in the company's proxy statement, and the remaining 19 went to a vote, with those voted on so far garnering average shareholder support of 13.8%. ISS recommended votes "against" all 11 advance notice bylaws proposals that received a recommendation as of June 1, 2023.

32 *Amazon.com, Inc.* (avail. Apr. 7, 2023, *recon. denied* Apr. 20, 2023)*.

33 For a detailed discussion of the SEC's universal proxy rules, *see SEC Adopts Rules Mandating Use of Universal Proxy Card*, Gibson Dunn (Nov. 18, 2021), *available here*.

D. The Return of Independent Board Chair Proposals

Although submissions focusing on governance topics were generally down this season, there was a significant increase in the number of proposals related to policies of separating the roles of chair of the board and CEO, which was the most frequent corporate governance proposal topic in 2023. There were 85 independent board chair proposals submitted this season, up from 50 proposals in 2022. Of the 85 independent board chair proposals submitted, at least 70 were submitted by John Chevedden and/or his associates, including Kenneth Steiner and Myra Young, and nine were submitted by the NLPC, which has historically not focused on the submission of proposals related to governance topics. Six proposals[34] were excluded via no-action requests, two on procedural grounds,[35] two on duplication grounds,[36] one on substantial implementation grounds,[37] and one on resubmission grounds.[38] The remaining 79 proposals were or will be voted on at company annual meetings, compared with only 40 proposals voted on in 2022. The 72 independent board chair proposals voted on so far this year received average shareholder support of 29.8%, in line with 2022 results, with no proposals receiving majority support. Notably, the proposals submitted by the NLPC received average shareholder support of 21.2%, compared to average shareholder support of 30.9% for the remaining proposals.

E. Increase in Proposals Focused on Shareholder Approval of Severance Agreements

Overall, the number of executive compensation shareholder proposals received by companies more than doubled this season. In 2023, 75 proposals focused on executive compensation were submitted, up from 36 proposals in 2022. This increase was largely attributable to the marked increase in proposals seeking shareholder approval of certain executive severance agreements, the most common executive compensation proposal received by companies.

Forty-seven proposals requesting boards seek shareholder approval of severance agreements were submitted in 2023, up markedly from 16 such proposals in 2022. These proposals typically requested that boards seek shareholder approval of any senior manager's new or renewed pay package that provided for severance or termination payments with an estimated value exceeding a certain multiple (usually 2.99x) of the executive's base salary and bonus. At least 43 of these 47 proposals were submitted by John Chevedden and/or his associates. Nine companies sought to exclude these proposals via no-action requests, seven of which were successful on procedural grounds.[39] The two remaining companies were denied relief, one arguing for exclusion on procedural grounds and one on substantial implementation grounds. Proposals seeking shareholder approval of severance agreements that went to a vote received average shareholder support of 23.8%, with two proposals receiving majority shareholder support. At numerous

[34] In one additional instance, the Staff concurred with exclusion of an independent chair proposal on procedural grounds, but the proposal was still included in the company's proxy statement and voted on. *See Laboratory Corp. of America Holdings (Chevedden)* (avail. Mar. 22, 2023).

[35] *The Allstate Corp.* (avail. Jan. 23, 2023); *Textron Inc.* (avail. Jan. 23, 2023)*.

[36] *PepsiCo, Inc.* (avail. Mar. 7, 2023)*; *Bank of America Corp. (Steiner)* (avail. Jan. 23, 2023)*.

[37] *Anavex Life Sciences Corp.* (avail. May 2, 2023).

[38] *CVS Health Corp. (Steiner)* (avail. Mar. 28, 2023).

[39] *Rite Aid Corp.* (avail. Apr. 12, 2023); *AMC Networks Inc.* (avail. Apr. 4, 2023); *JetBlue Airways Corp.* (avail. Jan. 19, 2023); *Kohls Corp.* (avail. Jan. 12, 2023); *The Walt Disney Co.* (avail. Dec. 5, 2022); *Visa Inc.* (avail. Nov. 8, 2022)*; *Walgreens Boots Alliance, Inc. (Chevedden)* (avail. Nov. 8, 2022)*.

companies, voting results were significantly affected by whether companies already had in place or, in response to the proposal, adopted policies addressing key aspects of the proposal.

F. Overall Decline in Civic Engagement Proposals but Congruency Proposals on the Rise

This season saw a decrease in the submission of proposals focusing on civic engagement, with the number of proposals addressing lobbying policies and practices disclosure, political contributions disclosure, and charitable contributions disclosure all declining (a total of 97 civic engagement proposals were submitted in 2023, compared to 106 in 2022). However, proposals focused on the alignment or congruency of a company's political contributions or lobbying expenditures with the company's publicly stated values saw an increase this season, with 21 such proposals submitted in 2023, compared to 14 such proposals in 2022.

Many of the new types of civic engagement shareholder proposals this season were ESG-skeptic proposals focused on the company's political speech or affiliations with certain entities. For example, NCPPR submitted six proposals requesting a report on the congruency of the company's partnerships with globalist organizations, expressing concerns about the company's affiliation with particular organizations (such as the World Economic Forum, Council on Foreign Relations, and Business Roundtable) that support stakeholder theory and that have agendas the proponent believes are incongruent with the company's fiduciary duty to shareholders. Three of these proposals went to a vote with the two voted on so far averaging support of 1.3%, and the remaining proposals were either excluded via no-action requests on procedural grounds or withdrawn. Other new proposals included three proposals submitted by The Bahnsen Family Trust relating to the company's involvement in "non-core" political issues (two of which were excluded via no-action request on ordinary business grounds and the other was withdrawn) and two proposals submitted by Ridgeline Research's American Conservative Values ETF requesting that companies encourage senior management to commit to avoiding political speech (both went to a vote with average support of 1.3%).

Overall, civic engagement proposals received average shareholder support of 22.9% in 2023. Thirty-four proposals focused on lobbying were submitted in 2023, compared with 46 proposals in 2022, with the 17 proposals that were voted on receiving average shareholder support of 32.9%, consistent with 33.1% support in 2022. Thirty proposals focused on political spending were submitted in 2023, compared with 36 proposals submitted in 2022, with the 12 proposals voted on receiving average shareholder support of about 20.6% (compared to 26.9% in 2022). Proposals focused on charitable contributions saw the biggest decrease in 2023, with three proposals submitted, compared with 13 in 2022, with the one that went to a vote receiving 7.4% shareholder support (compared to an average of 4.1% in 2022). Twenty-one proposals focused on congruency of political spending or lobbying with company values were submitted in 2023, compared with 14 in 2022, with the 13 voted on receiving average shareholder support of 19.1% (compared to 37.8% in 2022).

V. Other Important Takeaways from the 2023 Proxy Season

A. More Regulatory Change On the Horizon—Waiting on the SEC and Congress

1. SEC Amendment of Rule 14a-8

As discussed above, the 2023 proxy season was only the second season following the application of the Amended Rules, which were adopted by the SEC in September 2020. Following their adoption, opponents of the Amended Rules expressed concern that the increased stock ownership thresholds, additional procedural requirements, and higher resubmission thresholds could have a chilling effect on shareholders' ability "to use the shareholder proposal process to hold corporate boards and executives accountable on corporate governance and risk management."[40] However, those dire predictions have yet to materialize, as the impact of the Amended Rules has been relatively modest—shareholder proposal submissions have skyrocketed and exclusions on the basis of the Amended Rules have been relatively few and far between.[41]

Since the adoption of the Amended Rules, the pendulum has shifted in favor of shareholder proponents, as demonstrated by the Staff's issuance of SLB 14L in November 2021. And now more change is on the way in the form of significant amendments to Rule 14a-8 proposed by the SEC in July 2022 (the "2022 Proposed Amendments"). If adopted, the 2022 Proposed Amendments would formally modify three substantive bases for exclusion of shareholder proposals—substantial implementation, duplication, and resubmission.[42] In keeping with the thrust of SLB 14L and other efforts undertaken by the SEC since 2021, the 2022 Proposed Amendments would have the effect of further limiting the availability of these grounds for exclusion, likely leading to more shareholder proposals going to a vote.

a. Substantial Implementation

Under the current substantial implementation standard, a company may exclude a shareholder proposal "if the company has already substantially implemented the proposal."[43] The determination of whether a company has already substantially implemented a proposal tends to be fact-intensive, and the Staff has applied various interpretive frameworks when evaluating arguments for exclusion on this ground. Notably, however, under existing Staff guidance, a proposal "may be viewed as substantially implemented even if a company has not implemented all of the proposal's elements."[44] The 2022 Proposed Amendments would amend the language of Rule 14a-8(i)(10) to allow a company to exclude a proposal only "[i]f the company has already implemented the *essential elements* of the proposal" (emphasis added). Importantly, under the 2022 Proposed Amendments, substantial implementation would only be available if the company

[40] *See Investors and Consumer Groups Urge Members of Congress to Overturn Trump-Era SEC Rule Changes*, ICCR (Apr. 22, 2021), *available here*.

[41] For example, during the 2023 proxy season, only 11 proposals were excluded under the heightened requirements of the Amended Rules (three proposals were successfully excluded under the higher resubmission thresholds of the Amended Rules and eight proposals were excluded because proponents did not provide the required statement of engagement availability), representing only 1.2% of proposals submitted in 2023.

[42] *See* Release No. 34-95267 (the "2022 Proposing Release"), *available here*.

[43] Rule 14a-8(i)(10).

[44] 2022 Proposing Release at 12.

has implemented *all* of the proposal's essential elements. Moreover, the 2022 Proposing Release made clear that the concept of "essential elements" will be subjectively and broadly interpreted by the Staff. For example, a shareholder proposal requesting a report from a company's board of directors would not be excludable under the 2022 Proposed Amendments on substantial implementation grounds, even if the company publishes an identical report issued by the company's management, because the report did not come from the same entity requested in the proposal.

b. Duplication

The 2022 Proposed Amendments would also significantly change how the duplication standard under Rule 14a-8(i)(11) is applied. Under the existing standard, a company may exclude a shareholder proposal if it "substantially duplicates another proposal previously submitted to the company by another proponent that will be included in the company's proxy materials for the same meeting" so that shareholders will not have to consider two or more substantially identical proposals on the same ballot. When evaluating no-action requests arguing this ground, the Staff has historically considered whether the proposals share a common "principal thrust" or "principal focus." The 2022 Proposed Amendments would amend Rule 14a-8(i)(11) to provide that a proposal "substantially duplicates" another proposal if it "addresses the *same subject matter* and seeks the *same objective by the same means*" (emphasis added). Thus, in order to qualify for exclusion on this ground, proposals would need to more closely overlap and have both a shared objective and a shared approach for how that objective can be met.

c. Resubmissions

Finally, the 2022 Proposed Amendments would amend the framework used to analyze whether a proposal may be excluded under Rule 14a-8(i)(12), which allows a company to exclude a shareholder proposal that "addresses substantially the same subject matter" as a proposal, or proposals, that was previously included in the company's proxy materials within the past five calendar years and that proposal, or proposals, failed to achieve specified voting thresholds. Historically, the Staff has analyzed whether the proposals at issue share the same "substantive concerns," rather than the "specific language or actions proposed" to address those concerns. Under the 2022 Proposed Amendments, in order for a proposal to be eligible for exclusion under Rule 14a-8(i)(2) the proposal must "substantially duplicate" the prior proposal, not just "address substantially the same subject matter." Thus, just as with the proposed changes to Rule 14a-8(i)(11), the proposed changes to the resubmission analysis would require that a proposal "seek the same objective by the same means" as the prior proposal, or proposals. The proposed changes to the analysis of the resubmission basis will make it significantly harder for companies to exclude proposals, even when shareholders have recently expressed very low support for proposals addressing the same subject matter.

d. Timing of SEC Approval

The 2022 Proposed Amendments were listed on the SEC's Spring 2023 Unified Agenda of Regulatory and Deregulatory Actions (the "Reg Flex Agenda") when it was released on June 13, 2023.[45] The Reg Flex Agenda indicates that the 2022 Proposed Amendments remain in the Final Rule Stage and that the SEC is targeting adoption by October 2023. However, given the number of other pending rulemakings on the Reg Flex Agenda, including final adoption of the SEC's climate change rules and proposed rules for human capital management disclosure, it is unclear whether the SEC will meet its target date for adoption of the 2022 Proposed Amendments.

2. Congressional Efforts to Reform Rule 14-8

On February 3, 2023, House Financial Services Committee Chairman Patrick McHenry (R-NC) announced the formation of a Republican ESG Working Group, comprised of nine members and led by Representative Bill Huizenga (R-MI), "to combat the threat to our capital markets posed by those on the far-left pushing environmental, social, and governance (ESG) proposals.".[46] The Working Group was established to "[r]eign in the SEC's regulatory overreach; [r]einforce the materiality standard as a pillar of our disclosure regime; [a]nd hold to account market participants who misuse the proxy process or their outsized influence to impose ideological preferences in ways that circumvent democratic lawmaking."

In June 2023, the ESG Working Group released an interim report outlining the group's preliminary key priorities and issues identified to date.[47] The report identifies reforming the Rule 14a-8 no-action request process as a key priority of the Working Group's focus on reforming the proxy voting system for retail investors. The report posited that the "no-action letter process has become a mechanism for SEC staff to project its views about the 'significance' of non-securities issues, rather than a process for ensuring shareholder proponents' interests are aligned with those of their fellow shareholders."

With July 2023 declared "ESG Month"[48] by Representative Andy Barr (R-KY), several Congressional hearings have been held on ESG-skeptic topics, with more to come. At a July 12, 2023 hearing of the full House Financial Services Committee entitled "Protecting Investor Interests: Examining Environmental and Social Policy in Financial Regulation" scheduled for July 12, 2023,[49] the committee introduced 18 legislative proposals targeting what the hearing memorandum characterized as "[t]he federal government's focus on costly non-material environmental, social, and political issues at the expense of sound financial regulation," including actions by the SEC "that facilitate the inclusion of politically motivated shareholder

45 *Agency Rule List – Spring 2023 Securities and Exchange Commission, Office of Information and Regulatory Affairs* (2023), *available here*.

46 Press Release, *McHenry Announces Financial Services Committee Republican ESG Working Group* (Feb. 3, 2023), *available here*.

47 *Memorandum re Preliminary Report on ESG Climate Related Financial Services Concerns* (June 23, 2023), *available here*.

48 Eleanor Mueller, *The leader of the House GOP's anti-ESG efforts*, Politico (July 5, 2023), *available here*.

49 Press Release, *HEARING NOTICE: Protecting Investor Interests: Examining Environmental and Social Policy in Financial Regulation* (July 5, 2023), *available here*.

proposals in annual proxy statements and reversing important reforms to proxy solicitation rules."[50] Among the 18 legislative proposals are six bills targeting the shareholder proposal process. If adopted in their current form, the proposed bills would (1) nullify the 2022 Proposed Amendments;[51] (2) increase the resubmission thresholds under Rule 14a-8(i)(12);[52] (3) permit exclusion of shareholder proposals if the subject matter of the proposal is "environmental, social, or political (or a similar subject matter)";[53] (4) permit exclusion of a shareholder proposal under Rule 14a-8(i) "without regard to whether such shareholder proposal relates to a significant social policy issue";[54] (5) prohibit the SEC from compelling the inclusion or discussion of shareholder proposals in a company's proxy statement;[55] and (6) require the SEC to conduct a study of issues related to the proxy process, including issues related to the costs, risks and impacts of the shareholder proposal process on companies and the U.S. economy.[56] While it is unlikely that any of the proposed bills would be approved in the Senate and receive Presidential approval, these bills underscore that the shareholder proposal process will continue to be the focus of scrutiny from U.S. lawmakers throughout the 2024 proxy season and beyond.

B. Legal Challenges to the Rule 14a-8 Process

The 2023 proxy season saw a new challenge to the SEC Staff's role in the shareholder proposal process emerge in a lawsuit filed by NCPPR in the U.S. Court of Appeals for the Fifth Circuit. In *National Center for Public Policy Research v. SEC*, the Fifth Circuit is being asked to address several important questions about the Rule 14a-8 process, including: (1) whether responses to no-action requests issued by the Staff to companies that concur that a company may properly exclude a proposal under Rule 14a-8 are subject to judicial review; (2) the scope of the ordinary business exception under Rule 14a-8(i)(7); and (3) whether Rule 14a-8's requirement that, absent an exception, companies include shareholder proposals in their proxy statements exceeds the SEC's authority under the Exchange Act or violates the First Amendment.

The case arose out of a proposal submitted to The Kroger Co. requesting that the company issue a report "detailing the potential risks associated with omitting 'viewpoint' and 'ideology' from its written equal employment opportunity (EEO) policy." The Staff concurred with Kroger's no-action request, which argued that NCPPR's proposal could be excluded on ordinary business grounds.[57] In response, NCPPR filed a petition for review of the Staff's no-action decision in the Fifth Circuit and asked the court to stay the no-action decision during the litigation. According to NCPPR, by granting Kroger's no-action request, the SEC Staff's actions were arbitrary and capricious and constituted unconstitutional viewpoint discrimination, because the Staff has refused to grant no-action letters regarding similar proposals addressing other types of

[50] Committee Memorandum, *Financial Services Committee Hearing entitled "Protecting Investor Interests: Examining Environmental and Social Policy in Financial Regulation"* (July 7, 2023), *available here.*

[51] *Available here*.

[52] *Available here*.

[53] *Available here*.

[54] *Available here*.

[55] *Available here*.

[56] *Available here*.

[57] *The Kroger Co.* (avail. Apr. 12, 2023).

discrimination, such as discrimination based on race, sex, or sexual orientation.[58] In its response opposing the administrative stay granted by the Fifth Circuit, the SEC argued that the Fifth Circuit lacked jurisdiction to review the no-action decision (a) because a no-action decision represents an informal, non-binding determination by the Staff, rather than a formal, dispositive determination by the SEC itself, (b) because it is not a "final order[ ] of the Commission" subject to judicial review, and (c) because decisions about whether to initiate an enforcement action are committed to an agency's unreviewable discretion.[59]

After the Fifth Circuit referred the case to the merits panel, Kroger filed its final proxy materials, which included NCPPR's shareholder proposal.[60] Several weeks later, the National Association of Manufacturers ("NAM") intervened in the litigation. NAM raised a far-reaching challenge to the existing Rule 14a-8 framework, arguing that the requirement under Rule 14a-8 that companies include shareholder proposals in their proxy statements (absent an exception) exceeds the SEC's authority under the Exchange Act and asserting that statutory provision only authorizes the SEC to target misleading or deceptive statements by a company in its proxy statement. NAM further argued that, if Rule 14a-8 is statutorily authorized, it violates the First Amendment because the rule requires companies to speak on controversial topics and alters the content of their speech in contravention of the Constitution's restrictions on compelled speech and content-based speech regulations. The SEC subsequently filed a motion to dismiss the case, and on July 12, 2023, the Fifth Circuit entered an order declining to rule on the SEC's motions to dismiss the litigation, referring the motions to the merits panel, which will decide the case (including the threshold jurisdictional issues) after further briefing and argument. A decision will likely be issued in the spring or summer of 2024 at the earliest.

Given the broad scope of matters involved in this litigation, it is possible that the Staff may invoke its longstanding policy to express no view on a company's intention to exclude a shareholder proposal from its proxy materials where the company's arguments are being considered in a court of law.[61] For example, the Staff may determine to express no view (and thus not grant any no-action requests) on the application of the ordinary business rule generally or with respect to purportedly similar shareholder proposals (*e.g.*, nondiscrimination proposals) during the pendency of this litigation. This could result in a significant number of shareholder proposals (regardless of the proponent) being included in company proxy statements absent the company successfully negotiating with the shareholder proponent for the proposal to be withdrawn.

58 Notably, in 2022, the Staff permitted the exclusion of a substantially similar proposal submitted by NCPPR to BlackRock, Inc. on identical ordinary business grounds. *See BlackRock, Inc.* (avail. Apr. 4, 2022, *recon. denied* May 2, 2022).

59 The SEC emphasized that every court of appeals to consider the question has held that no-action requests are not final orders and therefore are not subject to judicial review, and that the appropriate procedure for NCPPR to seek relief would be to file a suit against Kroger in district court.

60 NCPPR's proposal was voted on at Kroger's 2023 annual meeting and received only 1.9% support.

61 The Staff took this approach, for example, in the early 1990s during litigation involving the application of the ordinary business exception to shareholder proposals requesting implementation of nondiscrimination policies, and more recently during the 2015 proxy season while the SEC was reconsidering the application of the conflicting proposals exception in Rule 14a-8(i)(9).

C. Shareholder Use of Exempt Solicitations Continues to Grow

The use of exempt solicitation filings by shareholder proponents continued to grow unabated in 2023, including as part of efforts to generate greater publicity for their proposals in advance of shareholders' meetings or to address other topics. Under Rule 14a-6(g) under the Exchange Act, shareholders owning more than $5 million of a company's securities generally must file a Notice of Exempt Solicitation (an "Exempt Notice") on EDGAR when soliciting other shareholders on a topic without seeking to act as a proxy. The rule is one of several exempting certain solicitations from the proxy filing requirements, and it was designed to address concerns that institutional investors and other large shareholders would conduct "secret" solicitations. However, in recent years, these filings have primarily been used by smaller shareholders to publicize their views on various proposals, as EDGAR does not restrict their use of these filings. In this regard, approximately 71% of Exempt Notices filed in 2023 were identified as voluntary filings by shareholders who did not own more than $5 million in company stock, down from 80% in 2022. As a result, it seems that shareholders continue to use these filings outside of Rule 14a-6(g)'s intended scope, resulting in some compliance issues and potential confusion for other shareholders when evaluating the items to be voted on.

As of June 1, 2023, there were a record-high 347 Exempt Notices filed since the beginning of the calendar year, up from 285 as of the same date in 2022 and 211 as of the same date in 2021. Frequent filers included As You Sow with 48 filings (up from 26 in 2022), NLPC with 29 filings (up from zero in 2022), John Chevedden with 28 filings (down from 30 in 2022), New York State Common Retirement Fund with 18 filings (up from two in 2022), and Majority Action, LLC with 16 filings (down from 26 in 2022). All of the Exempt Notices filed by As You Sow, NLPC, Mr. Chevedden, and Majority Action, LLC were voluntary.

While shareholder proponents have routinely used Exempt Notices to advocate for the proposals they submit, there was noteworthy evolution in the use of Exempt Notices during the 2023 proxy season—namely the use of Exempt Notices by intervening third-parties to express their views on shareholder proposals submitted by other shareholder proponents with whom they have no apparent relationship. For example, The International Brotherhood of Teamsters filed an Exempt Notice urging shareholders of Chipotle Mexican Grill, Inc. to support a shareholder proposal submitted by the Comptroller of the City of New York, As You Sow, and the New York City Retirement System requesting the company adopt a policy of non-interference with freedom of association rights.[62] Similarly, NLPC filed Exempt Notices in support of a number of proposals submitted by the American Conservative Values ETF. Notably, NLPC also filed Exempt Notices to voice its opposition to several proposals submitted by shareholder proponents, including three climate change proposals submitted by the New York State Common Retirement Fund, As You Sow, and Trillium Asset Management at Bank of America Corp.,[63] a proposal regarding lending and underwriting of fossil fuel exploration and development submitted by Harrington Investments, Inc. at Citigroup Inc.,[64] and a proposal requesting a report on the risks

62 *Available here.*

63 *Available here.*

64 *Available here.*

of doing business in states with restrictive abortion laws submitted by As You Sow at The Coca-Cola Co.[65]

Despite the continued growth in the use of exempt solicitations, the Staff has yet to address the continued potential for abuse. And that potential for abuse may be compounded if intervening third parties, who may or may not be shareholders, continue to use Exempt Notices to support or oppose shareholder proposals submitted by shareholder proponents.[66] We continue to recommend that companies both actively monitor their EDGAR file for these filings, review any Exempt Notices carefully and inform the Staff to the extent they believe an exempt solicitation filing contains materially false or misleading information or may not have been filed by a shareholder.[67]

D. Practice Pointers for the 2024 Proxy Season and Beyond

While the 2023 proxy season is just now concluding, companies should begin preparations for the 2024 proxy season now.

Companies should continue to monitor legislative, regulatory and other legal developments that may impact shareholder proposals during the 2024 proxy season. As noted above, following the Court's overturn of *Roe v. Wade* in 2022, the 2023 proxy season saw a renewed focus on shareholder proposals requesting a report on the effect of reproductive healthcare legislation. And most recently, the Court issued decisions on affirmative action at colleges and universities, ruling that institutions of higher education can no longer consider race in admissions decisions (subject to a narrow exception for remediating past discrimination) . It remains to be seen how the Court's decisions may impact shareholder proposals on DEI-related issues and companies' responses to such proposals in the coming proxy season.

As part of those preparations, companies would be well advised to review two key aspects of the deficiency notice process:

- *Review Language in Deficiency Notices*. In light of the Staff's focus on how companies explain procedural deficiencies, companies should carefully review their existing model language to assess whether it accurately and completely describes the requirements of Rule 14a-8. And when preparing deficiency notices for the 2024 proxy season, companies should take care to provide clear, plain English explanations of any identified procedural deficiencies.

- *Review Deficiency Notice Delivery Procedures.* As discussed above, the Staff is also keenly focused on the manner in which companies deliver deficiency notices to

[65] *Available here.*

[66] Unlike Exempt Notices filed by shareholder proponents, who were required to provide proof of their shareholder status when submitting their shareholder proposals, companies may be unable to confirm whether the intervening third parties are actually shareholders eligible to file Exempt Notices under Rule 14a-6(g).

[67] In 2018, the Staff published two new Compliance and Disclosure Interpretations ("C&DIs") providing some guidance on the use of Exempt Notices. Question 126.06 confirms the Staff's view that "voluntary" Notices of Exempt Solicitations can be filed, and Question 126.07 clarifies that each Notice of Exempt Solicitation, whether filed voluntarily or because it is required under Rule 14a-6(g), must include a notice page setting forth the information required under Rule 14a-103. Both C&DIs are available here.

shareholder proponents. Accordingly, companies should review their delivery procedures to assess whether, if challenged, they will have sufficient evidence to demonstrate that the proponent received the company's notice, even when the proponent claims otherwise.

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

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Glass Lewis Publishes Updates to 2024 U.S. Voting Policy Guidelines

Glass, Lewis & Co. ("Glass Lewis") recently published updates to its benchmark voting policy guidelines for U.S. companies, applicable to annual meetings of shareholders held starting January 1, 2024. In addition to various governance-related policy revisions and clarifying amendments to existing guidelines, Glass Lewis has made significant updates to several guidelines relevant to compensation committees. These updates, and their likely impact on 2024 annual meetings, are summarized below.

Compensation-Related Policy Updates and Clarifications

Compensation Recovery ("Clawback") Policies

In response to new NYSE and Nasdaq listing requirements related to compensation recovery ("clawback") policies, Glass Lewis updated its views on the utility of such policies. It believes that "effective" clawback policies should provide for the ability to clawback incentive-based compensation where there is evidence of problematic decisions or actions, such as material misconduct, material reputational failure, material risk management failure or a material operational failure, and the consequences of those decisions or actions are not already reflected in incentive payments. Further, it notes this right of clawback should be provided regardless of whether the employment of the subject executive was terminated, and if the company determines not to clawback compensation in these circumstances, it should disclose the rationale for that decision and alternative measures being taken, such as exercise of negative discretion in future payments. In short, Glass Lewis will likely raise concerns regarding clawback policies that only meet the basic requirements of the new NYSE and Nasdaq listing standards.

Stock Ownership Guidelines

Glass Lewis has codified its approach to stock ownership guidelines. It expects clear disclosure in the Compensation Discussion and Analysis of a company's required levels of ownership and how various equity awards are treated for determining compliance with those ownership levels. It explicitly notes that counting unearned performance-based full value awards and unexercised stock options is "inappropriate" and expects a "cogent rationale" if a company chooses to count these types of awards. While this change is significant for Glass Lewis, it matches the policy that Institutional Shareholder Services ("ISS") has had in place for several years. With both major proxy advisors now aligned on this subject, companies should review their current policies to determine whether updates may be warranted.

Board Oversight of Environmental and Social Issues

Given the importance of these issues to investors broadly, Glass Lewis believes oversight for these risks (which include risks stemming from topics often within the compensation committee's purview such as human capital, diversity, equity, inclusion and belonging and labor relations matters) should be formally codified in appropriate committee charters and other governing documents. It will be examining organizational documents across companies in the Russell 3000 index, and intends to recommend a vote against governance committee chairs at companies in the Russell 1000 index that fail to codify oversight of environmental and social risks. While its default voting recommendation is against nominating / governance committee chairs, this impacts compensation committees' charters and should be kept in mind when charters are next reviewed for updating.

Equity Award Proposals

Glass Lewis has added a new discussion relating to proposals seeking approval of an individual equity award, specifying that shareholders who would be recipients of the award are expected to abstain from voting. It emphasizes that doing so will be viewed positively in its analysis of the award, particularly where the recipient abstaining holds an ownership position that would materially influence the passage of the proposal.

Responsiveness Expectations, Including to Significant Say-on-Pay Opposition

Glass Lewis's threshold percentile for votes in opposition to management's recommendation that warrants responsive action by the board of directors remains unchanged at 20% for 2024. However, its updates clarify that in calculating this level of opposition (including against say-on-pay proposals) it includes both "Against" and "Abstain" votes. Practically, this means that it will calculate support levels using the following formula: [(For) / (For + Against + Abstain)], giving abstentions the effect of a vote against the proposal. Although abstentions often represent only a few percentage points for any given ballot item, this change elevates the level of support that companies will need to obtain for say-on-pay going forward.

Notably, Glass Lewis also removed shareholder proposals from its list of voting items that would warrant responsiveness above a 20% threshold, indicating that it no longer expects demonstrated responsiveness to shareholder proposals that cross a 20% support threshold. Its expectation of engagement with shareholders following a shareholder proposal that receives majority support remains unchanged.

Non-GAAP to GAAP Reconciliation Disclosure

Glass Lewis has expanded the discussion of its approach to the use of non-GAAP financial measures in incentive programs to emphasize the need for thorough and transparent disclosure in the proxy statement that will assist shareholders in reconciling the difference between non-GAAP results used for incentive payout determinations and reported GAAP results. Specifically, when significant adjustments were applied that materially impact incentive pay outcomes, the lack of such disclosure will impact Glass Lewis' assessment of the quality of a company's executive

Glass Lewis Publishes Updates to 2024 U.S. Voting Policy Guidelines (Continued)

pay disclosure and may be a factor in its vote recommendation on a say-on-pay proposal. We expect ISS will be making a similar change in its forthcoming 2024 policy updates, and encourage companies using non-GAAP financial measures to consider the need for disclosure enhancements in their 2024 proxy statements.

Use of SEC's "Pay-Versus-Performance" Disclosure Requirement

Glass Lewis notes that the "pay-versus-performance" disclosure requirement introduced in 2023 may be used as part of its supplemental quantitative assessments supporting the primary pay-for-performance grade. For example, the "compensation actually paid" data mandated by the SEC may be considered (along with other factors such as a realized pay analysis, overall incentive structure, the relevance of selected performance metrics, significant forthcoming enhancements, or reasonable long-term payout levels) and may give cause Glass Lewis to recommend in favor of a proposal even when it has identified a disconnect between pay and performance.

Governance-Related Policy Updates and Clarifications

Material Weaknesses

Glass Lewis will consider recommending votes against all members of the audit committee who served during the time when a material weakness was identified if a company has not disclosed a remediation plan, or when the material weakness has been ongoing for more than one year and the company has not disclosed an updated remediation plan that clearly outlines the company's progress toward remediating the material weakness.

Cyber Risk Oversight

Glass Lewis believes cyber risk is material for all companies, especially given the continued regulatory focus on, and potential adverse outcomes from, cyber-related issues. In instances where cyber-attacks have caused significant harm to shareholders, Glass Lewis will closely evaluate the board of directors' oversight of cybersecurity as well as the company's response and disclosures. In instances where a company has been materially impacted by a cyber-attack and Glass Lewis deems the board's oversight, response, or disclosures to be insufficient or not provided to shareholders, it may recommend a vote against appropriate directors.

Board of Directors' Diversity

Glass Lewis continues to tinker with its policies regarding diversity on the board of directors, making the following revisions for 2024:

- Gender and Underrepresented Community Diversity: Glass Lewis has clarified its policy on both board gender diversity and underrepresented community diversity to emphasize that when making director voting recommendations, it will carefully review a company's disclosure of its diversity considerations and may refrain from recommending that shareholders vote against directors when boards have provided a sufficient rationale or plan to address the lack of diversity on the board, including a timeline of when the board intends to appoint additional gender diverse and/or underrepresented community directors (generally by the next annual meeting of shareholders or as soon as reasonably practicable).
- Glass Lewis has revised its definition of "underrepresented community director" to replace its reference to an individual who self-identifies as gay, lesbian, bisexual, or transgender with an individual who self-identifies as a member of the LGBTQIA+ community.

Further Information

For more information on these updates and to view Glass Lewis' 2024 U.S. benchmark policy guidelines, click here

Need Assistance?

Compensia has extensive experience in helping companies understand and address proxy advisory firm and institutional shareholder voting and engagement policies, corporate governance, and executive compensation policies. If you have any questions on the topics covered in this Thoughtful Pay Alert or the Glass Lewis policies generally, please feel free to contact the authors of this Alert, Mark Borges at 415.462.2995 or mborges@compensia.com, Hannah Orowitz at 332.867.0566 or horowitz@compensia.com, or Alex Miller at 415.462.8918 or amiller@compensia.com.

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December 21, 2023

A Holiday Miracle? ISS Governance Announces 2024 Benchmark Policy Updates

Earlier this week, ISS Governance announced its 2024 Benchmark Policy Updates, which will be effective for meetings on or after February 1, 2024. In a miracle of miracles, no updates are contemplated for the US Benchmark Proxy Voting Guidelines. Instead, ISS Governance announced changes to its Canadian and Japan policies and Asia-Pacific regional markets policies. Appendix B to this summary shows there is just one clarification to the U.S. policy that codifies ISS's case-by-case approach on shareholder proposals to require shareholder ratification of executive severance arrangements or payments. I cannot remember if there was ever another time when ISS did not make any changes to its US benchmark proxy voting guidelines. Honestly, it feels kind of weird.

Of course, this outcome was foreshadowed last month when ISS Governance announced the launch of its open comment period on proposed changes to its benchmark voting policies. Notably, ISS Governance did not solicit comments for any policy changes in the US market.

– Dave Lynn

Posted by David Lynn
Permalink: https://www.thecorporatecounsel.net/blog/2023/12/a-holiday-miracle-iss-governance-announces-2024-benchmark-policy-updates.html

← Will Antitrust Scrutiny Curb E&S Activism? | Main | Voting Transparency: Norges' Pre-Meeting Disclosures Are Making an Impact →

January 4, 2024

More on ISS 2024 Benchmark Policy Updates: Just One Clarification to U.S. Policy

Here's something I shared early this week on the CompensationStandards.com Advisors' Blog:

In late December, Dave shared a holiday miracle on TheCorporateCounsel.net blog: ISS Governance announced its 2024 Benchmark Policy Updates effective for meetings on or after February 1, 2024, and no updates are contemplated for the U.S. Benchmark Proxy Voting Guidelines. There's only one clarification to the U.S. policy shown in Appendix B to this summary:

> [The clarification] codifies the case-by-case approach when analyzing shareholder proposals requiring that executive severance arrangements or payments be submitted for shareholder ratification. The updated policy (i) harmonizes the factors used to analyze both regular termination severance as well as change-in-control related severance (golden parachutes) and (ii) clarifies the key factors considered in such case-by-case analysis.

The edits resulting from this codification are detailed on page 3 of this document describing Benchmark Policy Changes for the Americas for 2024. The policy in effect for 2023 annual meetings stated that ISS would recommend voting for shareholder proposals requiring that golden parachutes or executive severance agreements be submitted for shareholder ratification unless they would require approval before entering into employment contracts. Then ISS would apply a case-by-case approach to the proposals to ratify or cancel golden parachutes. It also listed terms that an acceptable parachute should include.

The new policy reads as follows:

> Vote case-by-case on shareholder proposals requiring that executive severance (including change-in-control related) arrangements or payments be submitted for shareholder ratification.
>
> Factors that will be considered include, but are not limited to:
> – The company's severance or change-in-control agreements in place, and the presence of problematic features (such as excessive severance entitlements, single triggers, excise tax gross-ups, etc.);
> – Any existing limits on cash severance payouts or policies which require shareholder ratification of severance payments exceeding a certain level;
> – Any recent severance-related controversies; and
> – Whether the proposal is overly prescriptive, such as requiring shareholder approval of severance that does not exceed market norms.

– **Meredith Ervine**

Posted by Meredith Ervine
Permalink: https://www.thecorporatecounsel.net/member/blogs/proxy/2024/01/more-on-iss-2024-benchmark-policy-updates-just-one-clarification-to-u-s-policy.html

June 21, 2023

Self-Reporting Benefits Company in Latest Perks Enforcement Action

Yesterday, the SEC announced that it settled charges against a company and a former executive related to an alleged failure to disclose approximately $1.3 million worth of perquisites predominantly related to personal use of corporate aircraft by four of its executive officers and one of its directors over four years. During the years in question, the company's proxy did not disclose any compensation related to personal use of a corporate plane.

> The SEC's order against the company states that the company's process did not apply the "integrally-and-directly-related standard" to certain expenses, which resulted in the company understating the executives' and director's "All Other Compensation" by $325,000 per year, on average.
>
> In the SEC's order against the former executive, the SEC alleges that the executive failed to disclose approximately $280,000 in personal expenses charged to the company, including chauffer services, other travel, meals, apparel, and car repair services, in response to the company's D&O questionnaire and after reviewing drafts of the proxy statement. As a result of the executive's submission of these reimbursements and approval of payments to vendors, the company incorrectly recorded these as business expenses and not compensation.

Perks disclosure is technical, nuanced and, if the number of related enforcement actions is any indication, easy to get wrong. The SEC's order has a good reminder that the "integrally-and-directly-related standard" is very limited:

> According to the Adopting Release, even where the company "has determined that an expense is an 'ordinary' or 'necessary' business expense for tax or other purposes or that an expense is for the benefit or convenience of the company," that determination "is not responsive to the inquiry as to whether the expense provides a perquisite or other personal benefit for disclosure purposes." Indeed, "business purpose or convenience does not affect the characterization of an item as a perquisite or personal benefit where it is not integrally and directly related to the performance by the executive of his or her job."

While the perks footfault here may not be unusual, one notable aspect of this settlement is that the SEC declined to impose a civil penalty on the company, citing its self-reporting, cooperation and implementation of remedial measures. The former executive agreed to pay $75,000 in civil penalties to settle the charges.

– **Meredith Ervine**

Posted by Meredith Ervine
Permalink: https://www.compensationstandards.com/member/blogs/consultant/2023/06/self-reporting-benefits-company-in-latest-perks-enforcement-action.html

← Non-GAAP: Why Performance Metric Adjustments Might Differ From "Financial Reporting" Measures | Main | Climate Metrics: Rome Wasn't Built in a Day →

January 10, 2024

DEI Metrics: Measuring Progress in Non-Discriminatory Ways

I blogged last week on TheCorporateCounsel.net about changes to "corporate diversity" messaging that some companies are making in the wake of the SCOTUS ruling in *Students for Fair Admissions v. Harvard*. In our informal "Quick Poll," people were split on whether companies will soften DEI-related disclosures in proxy statements (feel free to add your two cents).

Over half of S&P 500 companies consider diversity metrics in some way in executive incentive plans, according to this WTW article. The article gives tips for how to respond to the ruling in the context of setting these goals. Here's an excerpt:

> **3. Be specific in measurement.** There are many ways DEI progress can be measured. While leadership and workforce representation goals may be a common approach, they also arguably present the highest reputational and litigation risk, especially if the company does not have strong documentation on career and pay decisions. Some other impactful ways to measure DEI progress include engagement score gaps for under-represented groups or participation in DEI enablement programs such as employee resource groups. In addition, companies should evaluate the pros and cons of using quantitative vs. qualitative measurement, especially in countries where demographic information is often self-reported and can be inaccurate. Companies that choose to assess DEI performance qualitatively should take note that investors strongly prefer quantitative and outcome-based metrics over activities-based and qualitative metrics.
>
> **4. Bolster the supporting infrastructure.** It is important to acknowledge that litigation risks with DEI programs have existed since before the SFFA decision, and many other corporate programs and policies are exposed to similar litigation risks. It is unrealistic to expect elimination of all risks associated with DEI programs, and companies should know that the benefits of DEI programs far outweigh the potential risks. A more reasonable approach is to proactively assess, quantify, and manage these risks. Companies should review practices in recruiting, career development, training and development, managerial enablement and performance management to ensure robust governance and documentation for how decisions are made and communicated.

I'll add my own tip, too: in addition to working with DEI practitioners, always consult an employment lawyer on this stuff!

– **Liz Dunshee**

Posted by Liz Dunshee
Permalink: https://www.compensationstandards.com/member/blogs/consultant/2024/01/dei-metrics-measuring-progress-in-non-discriminatory-ways.html

← DEI Metrics: Measuring Progress in Non-Discriminatory Ways | Main |

January 11, 2024

Climate Metrics: Rome Wasn't Built in a Day

This recent 9-page paper from Stanford's Rock Center for Corporate Governance looks at where practices stand for climate metrics in executive pay programs – and where they might be going. I blogged last month that "ESG" metrics, on the whole, are improving in the midst of pushback. In a similar vein, this paper says that setting climate goals and incorporating them into pay programs is a journey. Here's an excerpt:

> Most companies acknowledge that it takes time to learn how to break down multi-year targets into one-year goals. Through repeated effort, they learn how efficiency programs, sourcing programs, and technology translate into emission reductions. To many, the process is analogous to continuous improvement programs for capital efficiency. It also takes time to get the largest suppliers on board and to educate smaller suppliers on how they can reduce their carbon footprint.

And:

> Companies express very different experiences in the implementation of programs and creating buy in. For most, adopting climate targets and tying these to compensation is a multi-year (even decade-long) process. Companies newer to the effort will be faced with shorter timelines but have the benefit of learning from those who have gone before them. Companies phase the implementation, first adopting metrics to test their use and calculation before tying metrics to compensation. They also start at the top, adding climate goals to senior executive bonuses before rolling out to larger populations.

The underlying climate progress that the programs are intended to incentivize also takes time:

> While some companies aim to realize straight-line reductions (for example, 3 percent annual decreases in absolute terms), others are on a "hockey-stick" trajectory. Targets for the first five to seven years focus on the transition to renewable energy and gross energy reductions in production and supply. Beyond this, there is general acknowledgement that technological innovation (outside the company) is going to be required for companies to achieve their long-term pledges.

The paper gives practical suggestions on overcoming resistance to pay changes, board committee oversight practices, why this topic matters in the first place, and more. Here are recommended "best practices" for integrating climate goals into compensation:

> **1. Leadership and organizational commitment.** A company's commitment to decarbonization is most effective when leadership (CEO, senior executive team, and board) genuinely embraces climate goals. This includes prioritizing decarbonization so it is not seen as secondary to strategic and financial objectives but integral to them. Climate-related goals are tied to strategy, embedded in budgets, and ultimately made part of culture. The reasons that the organization has committed to climate goals should be clearly and consistently articulated to divisional leaders and within

functional groups to overcome resistance, remove inertia, and convince employees of the financial, organizational, and environmental necessity of decarbonization.

2. Metrics and reporting. Climate objectives should be few in number, low in redundancy, and largely quantifiable. We found that the most successful companies adopt science-based targets because of their demonstrable link to net-zero emission goals. Long-term targets are broken down into clearly achievable milestones, which map to quarterly, annual, and multi-year budgets and are supported by granular plans for capital allocation and procurement. Companies should be prepared to invest up front in systems for raw data collection and analytical processes, and entrust the reporting process to a small team of experts to ensure consistency and accuracy. Continuous improvement generally decreases cost and increase reliability over time. Ultimately, reported metrics should be audited to ensure accuracy and reliability.

3. Compensation. Climate programs are most effective when goals are added to executive and senior-manager compensation contracts to fully align the organization with its commitments. While many companies use the annual bonus program to do so, the most successful companies also embed climate in the longterm incentive program (LTIP) to match the timing of goals and compensation payouts. Annual targets in support of long-term goals are then reinforced through the annual incentive program. The achievement of annual goals gives executives and employees confidence that long-term objectives will be met. The rewards for meeting climate pledges should constitute a material part of at-risk compensation to encourage performance. Transparent reporting of interim and long-term targets allows the board and shareholders to monitor progress and hold the company accountable.

– **Liz Dunshee**

Posted by Liz Dunshee
Permalink: https://www.compensationstandards.com/member/blogs/consultant/2024/01/climate-metrics-rome-wasnt-built-in-a-day.html

August 30, 2023

Say-on-Pay: Investors Still Don't Like Time-Based "Special Awards"

We're nearing the end of August, and that means asset managers are sharing voting details for the past year. BlackRock shared in its 4th annual "voting spotlight" that where it did not support director elections or management proposals, compensation was one of the most common reasons. In the Americas, the BlackRock Investment Stewardship team voted against 243 directors based on compensation concerns.

In addition, both BlackRock & Vanguard have confirmed that they still aren't fond of special awards. From BlackRock:

> As we note in the BIS Global Principles, we are not supportive of one-off or special bonuses unrelated to company or individual performance. Where discretion has been used by the compensation committee or its equivalent, we look to the board to disclose how and why the discretion was used, and how the adjusted outcome is aligned with the interests of shareholders.
>
> As a result, BIS supported executive pay at fewer companies that made out-of-plan awards in 2022-23 proxy year because, in our view, these awards were increasingly unrelated to company performance and the financial interests of long-term shareholders like our clients.

As for Vanguard, it shared this cautionary tale in its investment stewardship report:

> At one company's 2023 annual meeting, the Vanguard-advised funds voted against Say on Pay because of concerns about the relative size of the pay program and the lack of performance conditions in a one-time equity grant. The CEO's five-year employment agreement provided for a $50 million special award of time-vesting restricted stock units. When evaluating these awards, we generally look for rigorous performance criteria as a requirement for vesting, as opposed to only the passage of time.

If the title of this blog looks familiar, it's because investors & proxy advisors said pretty much the same thing last year. BlackRock also commented earlier this year on how complex performance-based pay programs may be leading to more special awards – and I shared points to think about before heading down the "special award" path.

All that said, both asset managers were generally supportive of say-on-pay and other management compensation proposals over the past year. Vanguard also had this to say about the SEC's new "pay versus performance" rule:

> During engagements, company leaders and directors shared how they planned to modify their disclosures to improve the usefulness of their compensation-related disclosures to shareholders. On behalf of the Vanguard-advised funds, we support consistent, comparable disclosure.

– **Liz Dunshee**

Posted by Liz Dunshee

Permalink: https://www.compensationstandards.com/member/blogs/consultant/2023/08/say-on-pay-investors-still-dont-like-time-based-special-awards.html

← Cybersecurity Breaches: Adjustments to Earned Compensation | Main | Pay vs. Performance: Valuing "Retirement" Acceleration for CAP →

December 4, 2023

Equity Plan Approvals: Showing Signs of Headwinds?

According to a recent 12-page recap from WTW, this year has been relatively quiet when it comes to say-on-pay failures, with only 49 this year, compared to 69 last year and 60 in 2021. However, votes on equity plans indicate eroding support on that front. Here's an excerpt:

> We have observed some headwinds for equity plan share requests. We have observed one failure within the S&P 1500, similar to last year at this time (two failures at this time in 2021); however, ISS opposition is the highest at 17% compared with 13% at this time in 2022 and 2021. Support is at 89% compared with 91% at this time in 2022 and 2021.
>
> Companies should monitor their investors' voting guideline updates and engage with stakeholders to address proactively any potential issues anticipated ahead of planned stock plan proposals. With talent pressures continuing, companies should manage share pools to avoid unexpected surprises and factor any potential headwinds into their incentive programs.

WTW notes that these challenges come at the same time that companies may be needing to use more of their share pool to attract talent. This off-season will be a good time to monitor investor sentiment on dilution and provisions that are considered "problematic."

– **Liz Dunshee**

Posted by Liz Dunshee
Permalink: https://www.compensationstandards.com/member/blogs/consultant/2023/12/equity-plan-approvals-showing-signs-of-headwinds.html

← Cash Flows: Chief Accountant Says "Only Misclassification" Isn't a Persuasive Argument For Immateriality | Main | Form 8-K: Updated Reference Guides with New Item 1.05 →

December 7, 2023

Closest Thing to a Crystal Ball: Fall 2023 Reg Flex Agenda

Yesterday, the Fall 2023 Reg Flex Agenda was released. With two down and three to go, the list of rulemaking we've been tracking in the final rule stage is quite a bit shorter since the spring. All three have been pushed out to April. The proposed rulemaking we've been tracking is holding steady.

> Final Rule Stage
>
> – Climate Change Disclosure (April 2024)
> – Special Purpose Acquisition Companies (April 2024)
> – 14a-8 Amendments (April 2024)
>
> Proposed Rule Stage
>
> – Human Capital Management Disclosure (April 2024)
> – Regulation D and Form D Improvements (April 2024)
> – Revisions to the Definition of Securities Held of Record (April 2024)
> – Corporate Board Diversity (October 2024)
> – Rule 144 Holding Period (October 2024)

As a reminder, despite the title of this blog, these dates signify general timeframes! New final or proposed rules could come before the dates suggested in the agenda or be pushed out. This only gives insight into the priorities of the Chair as of the date it was submitted — it's not a definitive guide for anyone trying to predict SEC rulemaking for purposes of specific board agendas, budget and workflow. But we'll take any insight we can get!

– **Meredith Ervine**

Posted by Meredith Ervine
Permalink: https://www.thecorporatecounsel.net/blog/2023/12/closest-thing-to-a-crystal-ball-fall-2023-reg-flex-agenda.html

November 21, 2023

Form 10-K Human Capital Disclosures Continue to Evolve

A Survey of Disclosures from the S&P 100 During the Three Years Following Adoption of the Securities and Exchange Commission Rule

To Our Clients and Friends:

Human capital resource disclosures by public companies have continued to be a focus since the U.S. Securities and Exchange Commission (the "Commission") adopted the new rules in 2020; not only for companies making the disclosures, but employees, investors, and other stakeholders reading them. This alert updates the alert we issued in January 2023, "*Evolving Human Capital Disclosures: A Survey of Disclosures from the S&P 100 During the Two Years Following Adoption of the Securities and Exchange Commission Rule*," available here, and reviews disclosure trends among S&P 100 companies, each of which has now included human capital disclosure in their past three annual reports on Form 10-K. This alert also provides practical considerations for companies as we head into 2024.

The overall takeaway from our survey, which categorized disclosures into 27 topic areas, was that companies are generally tailoring the length of their disclosures and the topics covered and including slightly more quantitative information in some areas.[1] We note the following trends regarding the S&P 100 companies' disclosures compared to the previous year:

- *Length of disclosure.* Forty-eight percent of companies increased the length of their disclosures, four percent of companies' disclosures remained the same, and the remaining 48% of companies decreased the length of their disclosures (with the decreases generally attributable to the removal of discussion related to COVID-19).
- *Number of topics covered.* Twenty-two percent of companies increased the number of topics covered (with the categories seeing the most increases being diversity statistics by race/ethnicity and gender, employee mental health, monitoring culture, talent attraction and retention, and talent development), while 34% decreased the number of topics covered (the majority of which were attributable to the removal of disclosures related to COVID-19), and the remaining 46% covered the same number of topics.
- *Breadth of topics covered.* The prevalence of 16 topics increased, seven decreased, and four remained the same.
    - The most significant year-over-year increases in frequency involved the following topics: quantitative diversity statistics on gender (60% to 65%), employee mental health (46% to 50%), culture initiatives (22% to 26%), efforts to monitor culture (60% to 64%), and talent attraction and retention (90% to 94%).
    - The most significant year-over-year decrease involved COVID-19 disclosures, which declined in frequency from 69% to 34%. Other year-over-year decreases involved discussion of governance and organizational practices (56% to 51%) and diversity targets and goals (23% to 19%).
- *Most common topics covered.* The topics most commonly discussed this most recent year generally remained consistent with the previous two years. For example, diversity and inclusion, talent development, talent attraction and retention, and employee

compensation and benefits remained four of the five most frequently discussed topics, while quantitative talent development statistics, supplier diversity, community investment, and quantitative statistics on new hire diversity remained four of the five least frequently covered topics.

- *Industry trends.* Within the technology, finance, and energy industries, the trends that we saw in the previous year regarding the frequency of topics disclosed generally remained the same.

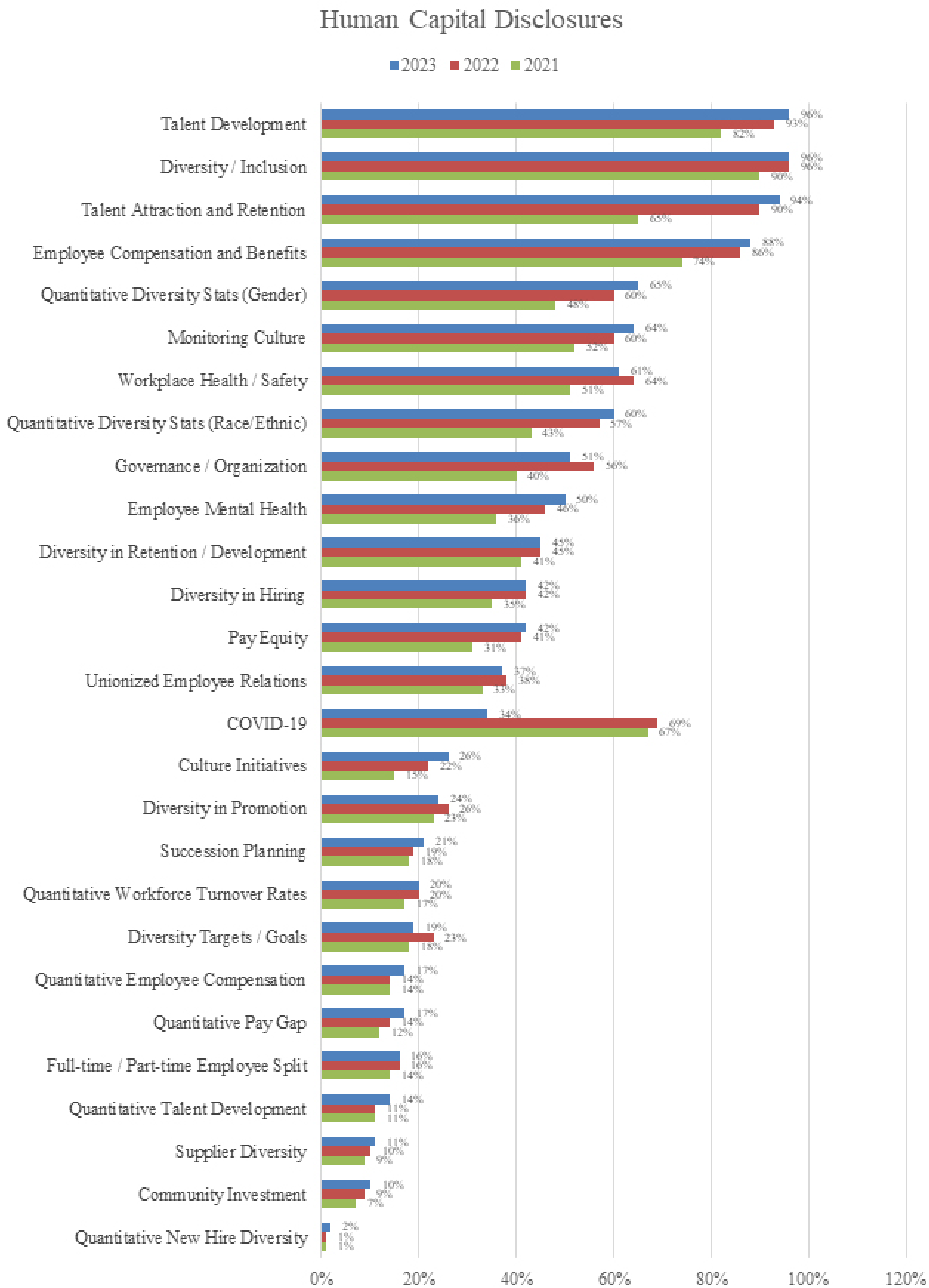
I. Background on the Requirements

On August 26, 2020, the Commission voted three to two to approve amendments to Items 101, 103, and 105 of Regulation S-K, including the principles-based requirement to discuss a registrant's human capital resources to the extent material to an understanding of the registrant's business taken as a whole.[2] Specifically, public companies' human capital disclosure must include "the number of persons employed by the registrant, and any human capital measures or objectives that the registrant focuses on in managing the business (such as, depending on the nature of the registrant's business and workforce, measures or objectives that address the development, attraction, and retention of personnel)."

Notably, the Commission's agenda list includes new human capital disclosure rules that are expected to be more prescriptive than the current rules, in part,[3] because one of the main criticisms of the existing human capital rules is lack of comparability across companies. Based on our survey, while company disclosures under the existing principles-based rules vary—which is expected under the principles-based regime—our survey was able to introduce some comparability. The next four sections show the relevant data from our survey.[4]

II. Disclosure Topics

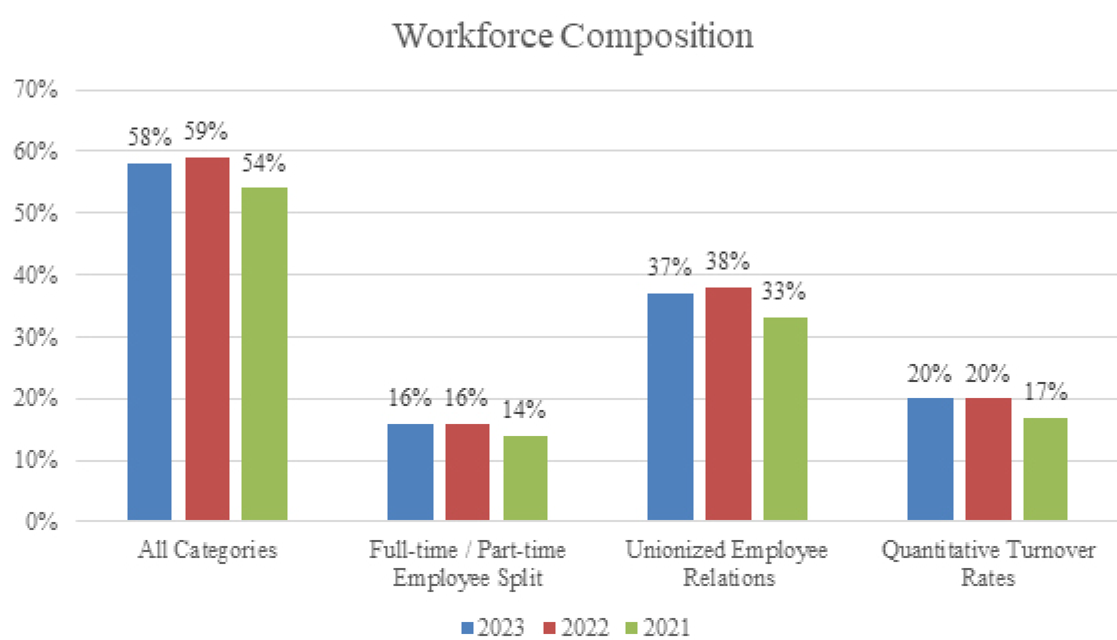
Our survey classifies human capital disclosures into 27 topics, each of which is listed in the following chart, along with the number of companies that discussed the topic in each of 2021, 2022, and 2023. Each topic is described more fully in the sections following the chart.


Human Capital Disclosures
2023
2022
2021
Talent Development
Diversity / Inclusion
Talent Attraction and Retention
Employee Compensation and Benefits
Quantitative Diversity Stats (Gender)
Monitoring Culture
Workplace Health / Safety
Quantitative Diversity Stats (Race/Ethnic)
Governance / Organization
Employee Mental Health
Diversity in Retention / Development
Diversity in Hiring
Pay Equity
Unionized Employee Relations
COVID-19
Culture Initiatives
Diversity in Promotion
Succession Planning
Quantitative Workforce Turnover Rates
Diversity Targets / Goals
Quantitative Employee Compensation
Quantitative Pay Gap
Full-time / Part-time Employee Split
Quantitative Talent Development
Supplier Diversity
Community Investment
Quantitative New Hire Diversity
0%
20%
40%
60%
80%
100%
120%

A. Workforce Composition

Among S&P 100 companies, 58% included disclosures relating to workforce composition in one or more of the following categories:

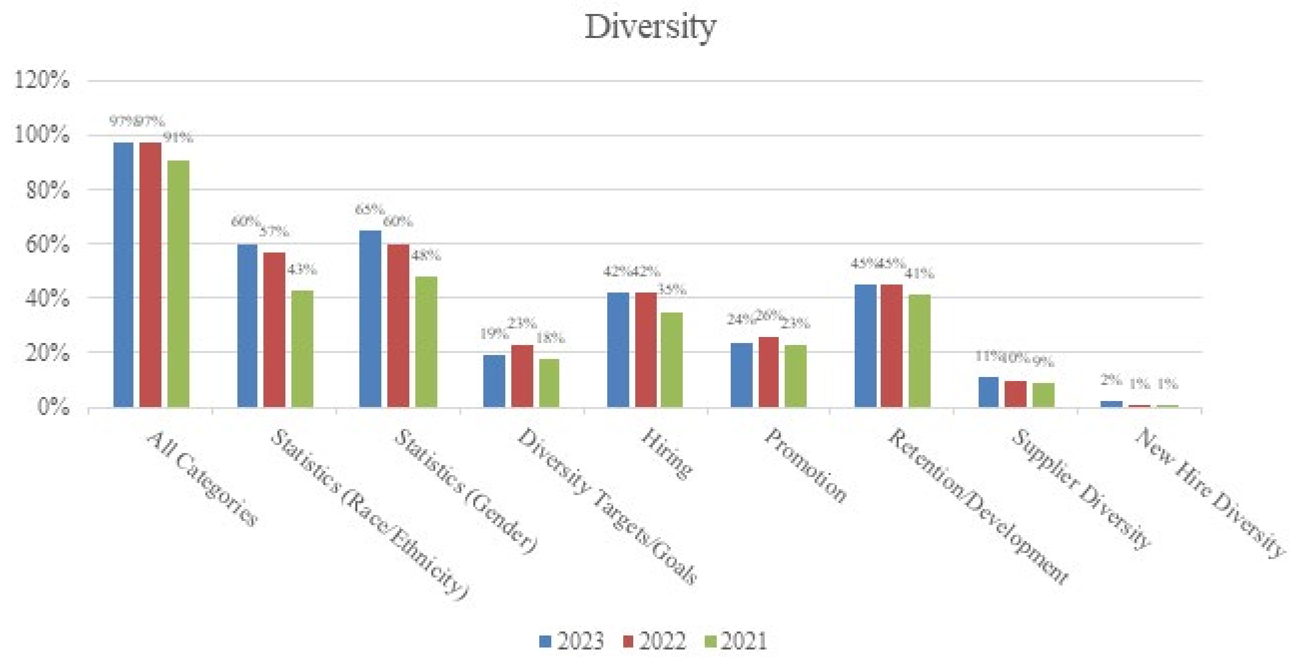
- ***Full-time/part-time employee split.*** While most companies provided the total number of full-time employees, only 16% of the companies surveyed included a quantitative breakdown of the number of full-time versus part-time employees, compared to the same percentage in the previous year and up slightly from 14% in 2021. Similarly, 67% of companies provided statistics on the number of seasonal employees and/or independent contractors or a breakdown of employees by business segment, job function, or geographical location, up from 65% in 2022 and 61% in 2021.
- ***Unionized employee relations.*** Of the companies surveyed, 37% stated that some portion of their workforce was part of a union, works council, or similar collective bargaining agreement, compared to 38% the previous year and 33% in 2021.[5] These disclosures generally included a statement providing the company's opinion on the quality of labor relations, and in many cases, disclosed the number of unionized employees.
- ***Quantitative workforce turnover rates.*** Although a majority of companies discussed employee turnover and the related topics of talent attraction and retention in a qualitative way (as discussed in Section II.B. below), only 20% of companies surveyed provided specific employee turnover rates (whether voluntary or involuntary), compared to the same percentage in the previous year and 17% in 2021.



B. Diversity

Among S&P 100 companies, 97% included disclosures relating to diversity in one or more of the following categories:

- ***Diversity and inclusion.*** This was the most common type of disclosure, with 96% of companies including a qualitative discussion regarding the company's commitment to diversity, equity, and inclusion ("DEI"), compared to the same percentage the previous year and up from 90% in 2021. The depth of these disclosures varied, ranging from generic statements expressing the company's support of diversity in the workforce to detailed examples of actions taken to recruit and support underrepresented groups and increase the diversity of the company's workforce.
- ***Priorities within diversity***. Companies disclosed different areas of focus for diversity efforts and programming within the organization. The most common disclosure was diversity in the retention or development of the company's current workforce (45% of companies surveyed in 2023, compared to 45% in 2022 and 41% in 2021), followed by diversity in the company's hiring practices (42% in 2023, compared to 42% in 2022 and 35% in 2021), followed by diversity in the company's promotion practices (24% in 2023, compared to 26% in 2022 and 23% in 2021), and then diversity in the company's suppliers (11% in 2023, compared to 10% in 2022 and 9% in 2021).
- ***Quantitative diversity statistics.*** Many companies also included a quantitative breakdown of the gender or racial representation of the company's workforce: 65% included statistics on gender and 60% included statistics on race or ethnicity (compared to 60% and 57% in 2022, respectively, and 48% and 43% in 2021, respectively). Companies provided gender statistics on both a global and U.S. basis, whereas nearly all companies provided race or ethnicity statistics for their U.S. workforce only. Most companies provided these statistics in relation to their workforce generally, regardless of position; however, an increased subset (40% in 2023, compared to 37% in 2022 and 26% in 2021) included separate statistics for different classes of employees (*g.*, managerial, vice president and above, etc.). Similarly, 10% of companies also provided separate statistics for their boards of directors (compared to 10% in 2022 and 4% in 2021). Some companies also included numerical goals for gender or racial representation, either in terms of overall representation, promotions, or hiring; 19% of companies included these diversity goals or targets (compared to 23% in 2022 and 18% in 2021).

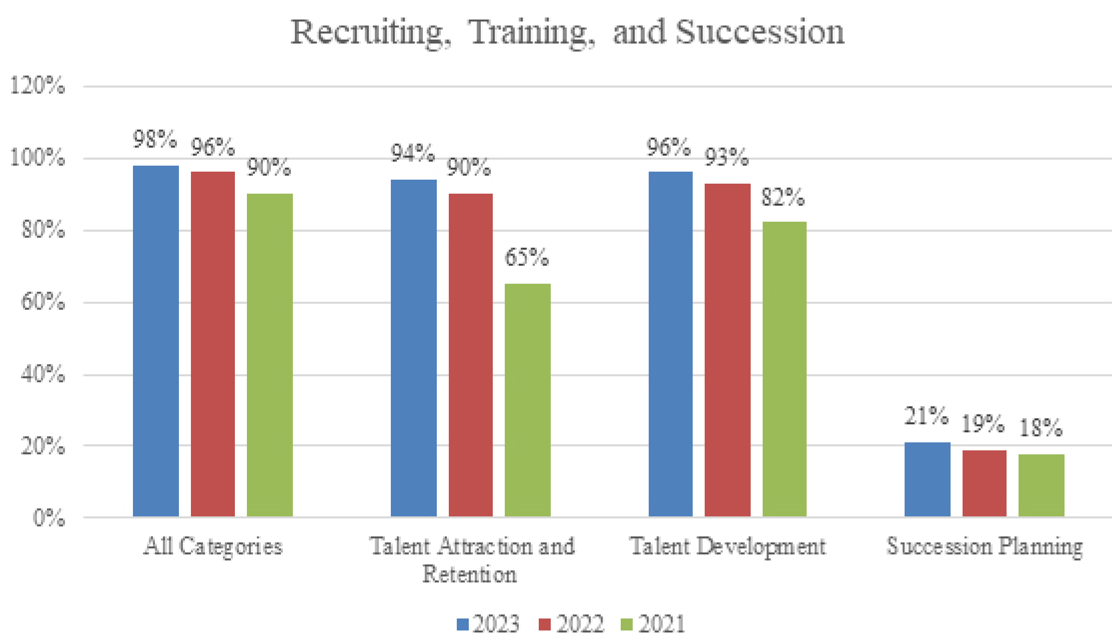


C. Recruiting, Training, Succession

Among S&P 100 companies, 98% included disclosures relating to talent and succession planning in one or more of the following categories:

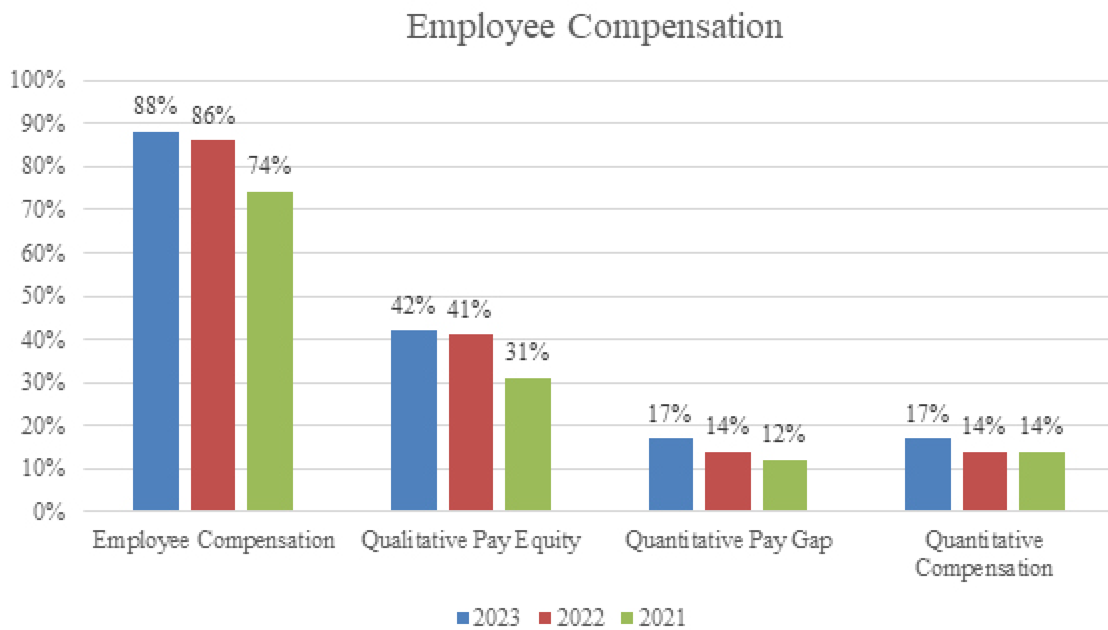
- ***Talent attraction and retention.*** These disclosures were generally qualitative and focused on efforts to recruit and retain qualified individuals. While providing general statements regarding recruiting and retaining talent were common, with 94% of companies including this type of disclosure (compared to 90% in 2022 and 65% in 2021), quantitative measures of retention, like workforce turnover rate, were uncommon, with only 20% of companies disclosing such statistics (as noted above).
- ***Talent development.*** Disclosures related to talent development were tied with talent attraction and retention as the most common category, with 96% of companies including a qualitative discussion regarding employee training, learning, and development opportunities, up from 93% the previous year and 82% in 2021. This disclosure tended to focus on the workforce as a whole rather than specifically on senior management. Companies generally discussed training programs such as in-person and online courses, leadership development programs, mentoring opportunities, tuition assistance, and conferences, and a minority also disclosed the number of hours employees spent on learning and development. Some companies discussed quantitative figures related to talent development, such as dollars or hours spent on training, with 14% of companies including this type of disclosure (compared to 11% in both 2022 and 2021).
- ***Succession planning.*** Only 21% of companies surveyed addressed their succession planning efforts (compared to 19% in 2022 and 18% in 2021), which may be a function

of succession being a focus area primarily for executives rather than the human capital resources of a company more broadly.



D. Employee Compensation[6]

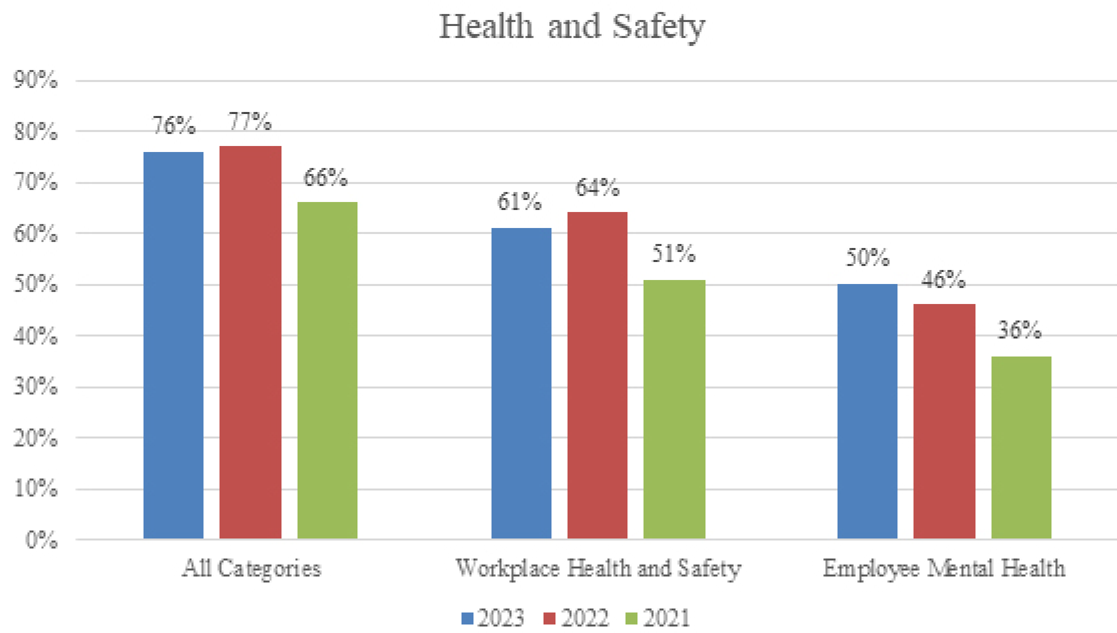
Among S&P 100 companies, 88% included disclosures relating to employee compensation, up from 86% the previous year and 74% in 2021. All of those companies included a qualitative description of the compensation and/or benefits program offered to employees. Of the companies surveyed, 42% addressed pay equity practices or assessments (up from 41% in 2022 and 31% in 2021), and substantially fewer companies included quantitative measures of the pay gap between racially or ethnically diverse and nondiverse employees or male and female employees (17% of companies surveyed in 2023, 14% in 2022 and 12% in 2021) or quantitative measures such as a minimum wage or investment in benefits (17% of companies surveyed in 2023, 14% in 2022, and 14% in 2021).



E. Health and Safety

Among S&P 100 companies, 76% included disclosures relating to health and safety in one or both of the following categories:

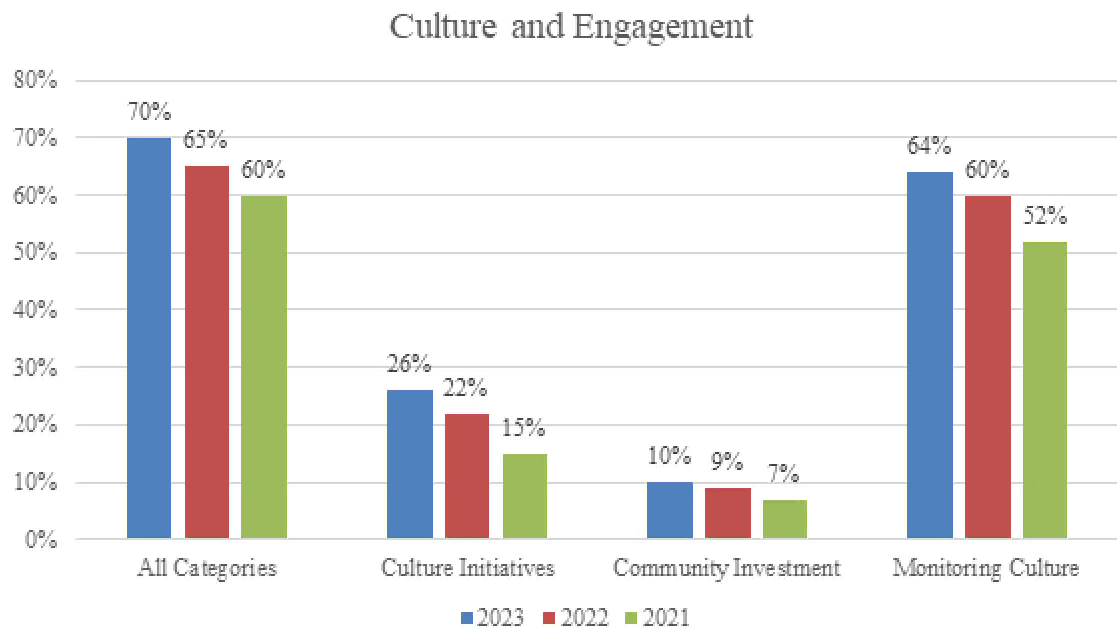
- ***Workplace health and safety.*** Of the companies surveyed, 61% included qualitative disclosures relating to workplace health and safety, down from 64% in the previous year but up from 51% in 2021, typically consisting of statements about the company's commitment to safety in the workplace generally and compliance with applicable regulatory and legal requirements. However, 8% of companies surveyed provided quantitative disclosures in this category (up from 7% in 2022 and 6% in 2021), generally focusing on historical and/or target incident or safety rates or investments in safety programs. These quantitative disclosures tended to be more prevalent among industrial, energy, and manufacturing companies. While many companies continued to provide disclosures on safety initiatives undertaken in connection with COVID-19, the decrease in safety disclosures in 2022 is largely due to the substantial decline in COVID-19 disclosures generally, which is discussed separately below.
- ***Employee mental health.*** In connection with disclosures about standard benefits provided to employees, or additional benefits provided as a result of the pandemic, 50% of companies disclosed initiatives taken to support employees' mental or emotional health and wellbeing, up from 46% the prior year and 36% in 2021.



F. Culture and Engagement

In addition to the many instances where companies mentioned a general commitment to culture and values, 70% of S&P 100 companies discussed specific initiatives they were taking related to culture and engagement in one or more of the following categories:

- ***Culture and engagement initiatives.*** Of the companies surveyed, 26% included specific disclosures relating to practices and initiatives undertaken to build and maintain their culture and values, up from 22% in the previous year and 15% in 2021. These companies most commonly discussed efforts to communicate with employees (*g.*, through town halls, CEO outreach, trainings, or conferences and presentations) and to recognize employee contributions (*e.g.*, awards programs and individualized feedback). Many companies also discussed culture in the context of diversity-related initiatives to help foster an inclusive culture.
- ***Community investment.*** Some companies disclose information about community investment, donations, or volunteer programs sponsored by the company, with 10% of companies surveyed providing such disclosure in 2023, compared to 9% in 2022 and 7% in 2021.
- ***Monitoring culture.*** Disclosures about the ways that companies monitor culture and employee engagement were much more common, with 64% of companies providing such disclosure, up from 60% the previous year and 52% in 2021. Companies generally disclosed the frequency of employee surveys used to track employee engagement and satisfaction, with some reporting on the results of these surveys, sometimes measured against prior year results or industry benchmarks.



G. COVID-19

The number of S&P 100 companies that included information regarding COVID-19 and its impact on company policies and procedures or on employees generally declined sharply, with 34% of companies making such disclosure, compared to 69% in 2022 and 67% in 2021. COVID-19-related topics addressed ranged from work-from-home arrangements and safety protocols taken for employees who worked in person to additional benefits and compensation paid to employees as a result of the pandemic and contributions made to organizations supporting those affected by the pandemic. This sharp decline in COVID-19 disclosures is consistent with a more general trend of companies discussing COVID-19 less frequently as a result of its decreasing significance and illustrates the expected evolution of disclosure resulting from a principles-based framework.

H. Human Capital Management Governance and Organizational Practices

Over half of S&P 100 companies (51% of those surveyed, compared to 56% in 2022 and 40% in 2021) addressed their governance and organizational practices (such as oversight by the board of directors or a committee and the organization of the human resources function).

III. Industry Trends

One of the main rationales underlying the adoption of principles-based—rather than prescriptive—requirements for human capital disclosures is that the relative significance of various human capital measures and objectives varies by industry. This is reflected in the following industry trends that we observed:[7]

- ***Technology Industries*** *(E-Commerce, Internet Media & Services, Hardware, Software & IT Services, and Semiconductors).* For the 21 companies in the Technology Industries, at least 85% discussed each of talent development and training opportunities, talent attraction, recruitment and retention, employee compensation, and diversity. Compared to the S&P 100 as a whole, relatively uncommon disclosures among this group included part-time and full-time employee statistics (5%), succession planning (10%), COVID-19 (24%), supplier diversity (5%), and unionized employee relations (19%). However, these industries saw increased rates of disclosure compared to the S&P 100 for quantitative turnover rates (43%) and qualitative pay equity (57%).
- ***Finance Industries*** *(Asset Management & Custody Activities, Consumer Finance, Commercial Banks, and Investment Banking & Brokerage).* For the 13 companies in the Finance Industries, a large majority included quantitative diversity statistics regarding race (85%) and gender (92%) and qualitative disclosures regarding employee compensation (92%), and, compared to other industries, a relatively higher number discussed pay equity (62%) and quantified their pay gap (38%). Relatively uncommon disclosures among this group included part-time and full-time employee statistics, unionized employee relations, quantitative workforce turnover rates, and succession planning (in each case less than 16%).
- ***Energy Industries*** *(Oil & Gas Exploration & Production and Electric Utilities & Power).* For the seven companies in the Energy Industries, a large majority included quantitative diversity statistics regarding race (71%) and gender (86%), qualitative disclosures regarding employee compensation (86%), and governance and organizational practices (71%), and, compared to other industries, a relatively higher number discussed unionized employee relations (57%) and quantified their workforce turnover rates (57%). Relatively uncommon disclosures among this group included part-time and full-time employee statistics, diversity in promotion, diversity targets or goals, culture initiatives, quantitative employee compensation statistics, pay equity, and quantitative pay gap (in each case less than 15%).

IV. Disclosure Format

The format of human capital disclosures in S&P 100 companies' annual reports on Form 10-K continued to vary greatly.

Word Count. The length of the disclosures ranged from 106 to 2,094 words, with the following statistical trends in the past three years:

	2023	2022	2021
Minimum word count	106	109	105
Maximum word count	2,094	1,995	1,931
Median	1,025	949	818
Mean	987	964	828

Metrics. The disclosure requirement specifically asks for a description of "any human capital *measures* or objectives that the registrant focuses on in managing the business" (emphasis added). Our survey revealed that companies are increasingly providing quantitative metrics, with 85% of companies providing disclosure in at least one of the quantitative categories we discuss above (up from 82% in 2022 and 68% in 2021) and only 5% electing not to include any type of quantitative metrics beyond headcount numbers (down from 8% in 2022 and 12% in 2021). The group of companies that identify important objectives they focus on but omit quantitative measures related to those objectives has been shrinking as more companies choose to include metrics. For example, 96% of companies discussed their commitment to diversity, equity, and inclusion (compared to 96% in 2022 and 89% in 2021), and 65% and 61% of companies disclosed quantitative metrics regarding gender and racial diversity, respectively (compared to 60% and 58%, respectively, in 2022 and 47% and 43%, respectively, in 2021).

Graphics. Although the minority practice, 27% of companies surveyed also included tables, charts, graphics or similar formatting used to draw attention to particular elements, up from 24% the previous year and 21% in 2021, which were generally used to present statistical data, such as diversity statistics or breakdowns of the number of employees by geographic location. *Categories.* Most companies organized their disclosures by categories similar to those discussed above and included headings to define the types of disclosures presented.

V. Upcoming Rulemaking and Investor Advisory Committee Recommendations

At its meeting on September 21, 2023, the Commission's Investor Advisory Committee ("IAC") approved subcommittee recommendations (the "IAC Recommendations") to expand required human capital management disclosures.[8] The Commission must now decide whether to incorporate the IAC Recommendations into its anticipated human capital management rule proposal, which according to the most recent Regulatory Flexibility agenda, which is admittedly aspirational, was expected to be issued in October.[9]

The IAC Recommendations contain prescriptive disclosure requirements—many of which have been previously considered as part of the 2020 rulemaking—for various quantitative metrics in the business description of Form 10-K under Item 101(c) of Regulation S-K as well as narrative disclosure in Management Discussion and Analysis. The recommended changes to Item 101(c) would require disclosure of the following metrics:

- ***Headcount Metrics.*** Companies would be required to disclose "[t]he number of people employed by the issuer, broken down by whether those people are full-time, part-time, or contingent workers." This disclosure would include "reporting on all similarly situated persons whose work contributes to a material level of revenue or income."
- ***Turnover Metrics.*** Companies would be required to disclose "turnover or comparable workforce stability metrics." The IAC Recommendations do not address whether the calculation of turnover would be determined by the SEC or by companies individually.
- ***Components of Compensation.*** The IAC Recommendations also require disclosure of "[t]he total cost of the issuer's workforce, broken down into major components of compensation." This would require companies to break out each component of labor costs (*g.*, salary, equity, etc.), rather than aggregating labor costs with other line-item expenses, such as cost of goods sold or selling, general, and administrative costs, on the companies' income statements.

- ***Demographic Data.*** Companies would also be required to disclose "[w]orkforce demographic data sufficient to allow investors to understand the company's efforts to access and develop new sources of talent, and to evaluate the effectiveness of these efforts." This disclosure would include "diversity across gender, race/ethnicity, age, disability, and/or other categories viewed as important to investors and relevant to the business" and "diversity at senior levels." The IAC Recommendations includes a brief reference in a footnote that any new rules could provide a "limited exception for disclosure of workforce composition outside the United States to consider laws and regulations in non-U.S. jurisdictions" without providing any additional guidance.

The recommended narrative disclosure in MD&A would discuss how the company's "labor practices, compensation incentives, and staffing fit within the broader firm strategy. Such a discussion would address what portion of labor costs management views as an investment and why, including how labor is allocated across areas designed to promote firm growth (e.g., R&D) and those necessary to maintain current operations rather than increase sales revenue (e.g., compliance)."

While one of the key criticisms of the current rule appears to be lack of standardized disclosure that would allow for greater comparability among companies, it is not clear that human capital disclosures that are material to each company can be truly standardized given the different industries, sizes, geographic reach, and other qualities of public companies. As shown by the data discussed above, in response to the 2020 principles-based rules, public companies are providing more robust human capital disclosures in their SEC filings and are continuing to evolve these disclosures with each filing.

VI. <u>Comment Letter Correspondence</u>

Comment letter correspondence from the staff of the Division of Corporation Finance (the "Staff"), which often helps put a finer point on principles-based disclosure requirements like this one, has shed relatively little light on how the Staff believes the new requirements should be interpreted. Consistent with what we found at this time last year and the year before, the comment letters, all of which involved reviews of registration statements, were generally issued to companies whose disclosures about employees were limited to the bare-bones items companies have discussed historically, such as the number of persons employed and the quality of employee relations. From these companies, the Staff simply sought a more detailed discussion of the company's human capital resources, including any human capital measures or objectives upon which the company focuses in managing its business. There were also a few comment letters where the Staff asked companies to clarify statements in their human capital disclosures. Based on our review of the responses to those comment letters, we have not seen a company take the position that a discussion of human capital resources was immaterial and therefore unnecessary.

VII. <u>Implications of Recent U.S. Supreme Court Decisions</u>

On June 29, 2023, the United States Supreme Court released its opinion in *Students for Fair Admissions v. Harvard*, in which the Court held that Harvard's and the University of North Carolina's use of race in their admissions policies was unlawful. Although the Supreme Court's holding addressed only college and university admissions and not private-sector employers, the increased scrutiny on affirmative action programs in the workplace in the wake of *SFFA* has heightened the risk that employers with robust DEI initiatives may face litigation from employees, potential contracting partners, advocacy groups, and government agencies. Since the *SFFA* opinion was released, advocacy groups have sent dozens of letters to companies claiming that their DEI programs violate federal antidiscrimination law, including Title VII (discrimination in employment) and Section 1981 (discrimination in contracting), and arguing that the legal risk associated with DEI programs threatens stockholders' value, and a number of lawsuits have been filed. Many companies are carefully reviewing their DEI programs and related public disclosures in light of these risks. For more information on the latest DEI developments, please see our DEI Task Force newsletter here.

VIII. Conclusion

Based on our survey, companies continue to be thoughtful about their human capital disclosures—expanding their disclosures in some areas (*e.g.*, quantitative diversity statistics on gender) and reducing them in others (*e.g.*, COVID-19)—in response to ever-changing circumstances. That is precisely what principles-based disclosure rules are designed to elicit. To that end, as companies prepare for the upcoming Form 10-K reporting season, they should consider the following:

- Confirming (or reconfirming) that the company's disclosure controls and procedures support the statements made in human capital disclosures and that the human capital disclosures included in the Form 10-K remain appropriate and relevant. In this regard, companies may want to compare their own disclosures against what their industry peers did these past three years, including specifically any notable additional disclosures made in the past year.
- Reviewing disclosures in light of the IAC Recommendations to assess whether any of the human capital measures or objectives may be material to the company.
- Setting expectations internally that these disclosures likely will evolve. As shown by the measurable increase in disclosure in the third year of reporting, companies should expect to develop their disclosure over the course of the next couple of annual reports in response to peer practices, regulatory changes, and investor expectations, as appropriate. The types of disclosures that are material to each company may also change in response to current events, as was shown by the sharp decrease in COVID-19 related disclosures this past year.
- Addressing in the upcoming disclosure, if not already disclosed, the progress that management has made with respect to any significant objectives it has set regarding its human capital resources as investors are likely to focus on year-over-year changes and the company's performance versus stated goals.
- Addressing significant areas of focus highlighted in engagement meetings with investors and other stakeholders. In a 2021 survey, 64% of institutional investors surveyed cited human capital management as a key issue when engaging with boards (second only to climate change at 85%).[10]
- Revalidating the methodology for calculating quantitative metrics and assessing consistency with the prior year. Former Chairman Clayton commented that he would expect companies to "maintain metric definitions constant from period to period or to disclose prominently any changes to the metrics."

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[1] Data provided is as of November 3, 2023. The categorization data necessarily involves subjective assessment and should be considered approximate.

[2] *See* 17 C.F.R. § 229.101(c)(2)(ii).

[3] *Agency Rule List – Spring 2023 Securities and Exchange Commission, Office of Information and Regulatory Affairs* (2023), *available* here.

[4] Note that companies often include additional human capital management-related disclosures in their ESG/sustainability/social responsibility reports, on their websites, and in their proxy statements, but these disclosures are outside the scope of the survey, which is focused on disclosures included in Part I, Item 1 of annual reports on Form 10-K.

[5] While never expressly required by Regulation S-K, as a result of disclosure review comments issued by the Division of Corporation Finance over the years and a decades-old and since-deleted requirement in Form 1-A, it has been a relatively common practice to discuss collective bargaining and employee relations in the Form 10-K or in an IPO Form S-1, particularly since the threat of a workforce strike could be material.

[6] Our survey reviewed the employee compensation disclosures contained in Part I, Item 1 of each company's Form 10-K and did not separately review any employee compensation information included in companies' financial statements or the notes thereto.

[7] For purposes of our survey, we grouped companies in similar industries based on both their four-digit Standard Industrial Classification code and their designated industry within the Sustainable Industry Classification System. The industry groups discussed in this section cover 41% of the companies included in our survey.

[8] *Available at* https://www.sec.gov/files/spotlight/iac/20230921-recommendation-regarding-hcm.pdf.

[9] *Agency Rule List – Spring 2023 Securities and Exchange Commission, Office of Information and Regulatory Affairs* (2023), *available* here.

[10] *See* Morrow Sodali 2021 Institutional Investor Survey, *available at* https://morrowsodali.com/insights/institutional-investor-survey-2021.

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