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GLOBAL PUBLIC COMPANY ACADEMY

2023 Proxy Season: A Recap of 2022 and Trends to Watch

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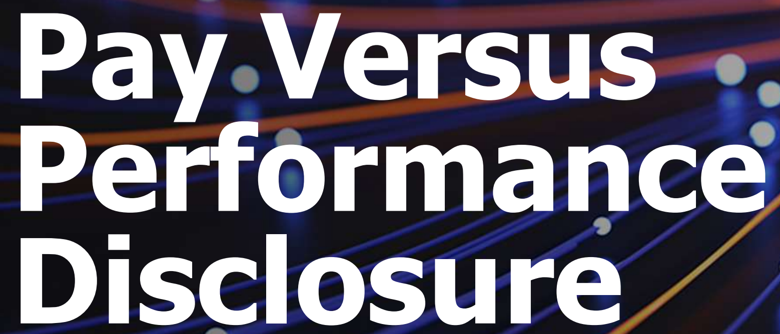
Pay Versus Performance Disclosure



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New SEC Disclosure Rules

- On August 25, 2022, the SEC adopted new rules to require enhanced pay for performance disclosure that will apply to 2023 proxies for calendar year-end companies.
  - Registrants are required to comply with the new amendments in proxy and information statements that are required to include Item 402 executive compensation disclosure for fiscal years ending on or after December 16, 2022.
- New Item 402(v) of Regulation S-K requires companies to provide a table disclosing specified executive compensation and financial performance measures for their five most recently completed fiscal years.
  - Registrants may provide the disclosure for three years instead of five years in the first filing in which they provide pay versus performance disclosure, per Instruction 1 to Item 402(v).

Pay Versus Performance Disclosures

- New Item 402(v) requires:
  1. A tabular disclosure containing executive compensation and financial performance metrics, in each case over the last five fiscal years;
  2. A clear description, either in narrative or graphical format, of the relationships between
     a) each of the financial performance measures included in the table and
     b) the executive compensation actually paid to the PEO and, on average, to the other NEOs; and
  3. A list of three to seven financial performance measures (the "Tabular List") that the registrant believes are its most important measures to link pay and performance, using the same approach as taken for the Company-Selected Measure.

Pay Versus Performance Table

The table required under new Item 402(v) requires disclosure containing the following information, in each case over the last five fiscal years:

1. "Total" compensation (using the Summary Compensation Table measure of total compensation)

2. Quantitative information reflecting "executive compensation actually paid" to NEOs, which is required on an individual basis for the PEO and as an average for the other NEOs

3. TSR for both the registrant and its peer group, based on a fixed $100 investment

4. The registrant's net income

5. A "Company-Selected Measure," which is a financial performance measure chosen by, and specific to, the registrant that represents, in the registrant's view, the most important financial performance measure it uses to link NEO pay and performance for the most recently completed fiscal year

New Item 402(v) Pay Versus Performance Table

PAY VERSUS PERFORMANCE								
Year (a)	Summary Compensation Table Total for PEO (b)	Compensation Actually Paid to PEO (c)	Average Summary Compensation Table Total for Non-PEO Named Executive Officers (d)	Average Compensation Actually Paid to Non-PEO Named Executive Officers (e)	Value of Initial Fixed $100 Investment Based On:		Net Income (h)	[Company-Selected Measure] (i)
					Total Shareholder Return (f)	Peer Group Total Shareholder Return (g)		

Company-Selected Measure

- The Company-Selected Measure must reflect the registrant's assessment that it is the most important performance measure (that is not otherwise required to be disclosed in the tabular disclosure required under Item 402(v) (i.e., TSR or net income)) for linking pay and performance.
- If the registrant's "most important" measure is already included in the Item 402(v) tabular disclosure (i.e., TSR or net income), the registrant would select its next most important measure as its Company-Selected Measure.
- Company-Selected Measures may differ from one year to the next.
- The Company-Selected Measure must be a financial performance measure included in the Tabular List.

Calculating Compensation Actually Paid

- The purpose of the disclosure is to show the value of compensation actually paid as compared to the company's financial performance.
- Compensation actually paid as calculated under these new rules is not the same as realized pay or even pay that has been received by these individuals during the prescribed year.
- For equity awards, the disclosure reflects incremental changes in value from the base value established in the year the award is granted.
- The cumulative value disclosed for each award should be equal to the final value as of the vesting date.

Compensation Elements

The calculation includes the following three elements:

Cash compensation

Essentially the same as what is reported in the Summary Compensation Table.

Defined benefit pensions

Instead of using the change in pension value reported in the Summary Compensation Table, this calculation requires companies to calculate the pension service cost for the year.

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Equity compensation

The rules require a very different approach than the 2015 proposed rules, which would have valued equity at vesting. The calculation is similar to the calculation of "realizable pay" but essentially marks to market unvested and outstanding equity awards based on their fair value from the grant date to the vesting date.

Description of Relationship Between Compensation and Performance

- Companies must provide a clear description, either in narrative or graphical format, of the relationships between
  - each of the financial performance measures included in the table, and
  - the executive compensation actually paid to the PEO and, on average, to the other NEOs.
- Companies must also describe the relationship between the registrant's TSR and its peer group TSR.

Tabular List

- Companies must also provide a list of three to seven financial performance measures that the company believes are its most important measures to link pay and performance, using the same approach as taken for the Company-Selected Measure.
- Companies are permitted, but not required, to include nonfinancial measures in the Tabular List if they consider such measures to be among their three to seven “most important” measures.
- Companies may provide the Tabular List disclosure as a single list, as two separate lists (one for the PEO and one for all NEOs other than the PEO), or as separate Tabular Lists for the PEO and each NEO other than the PEO.

Challenges with the Disclosure Requirement

No real "grace period" for implementing the disclosure

Companies are not used to having to revalue their equity awards following the grant date fair value

TSR as a challenge:

- Many companies historically have not used TSR within their CD&A
- Against the backdrop of the current macroeconomic environment – which is disparately impacting certain industries – TSR may look particularly challenged for certain companies as compared to the selected peer group

Time/expense associated with calculating the amounts to be shown in the table

Will this disclosure –

- Adversely impact say-on-pay results?
- Invite questions from activist stockholders or others as to why a company chooses a particular "Company-Selected Measure" that differs from the peer group?

Placement of Pay Versus Performance Disclosure

- New Item 402(v) does not specify the location of the new disclosure within the proxy statement.
  - It does **not** have to be contained in the CD&A
- SEC noted that mandating pay versus performance disclosure in the CD&A section of the proxy statement may cause confusion by suggesting that the company considered the pay versus performance relationship in its compensation decisions.
- Typically, the CD&A information doesn't relate to compensation "actually paid," so there could be a mismatch (real or perceived) by including this information within the CD&A.

Non-GAAP Financial Measures

- Companies may opt to provide a non-GAAP financial measure as their Company-Selected Measure (or as one of the additional measures).
- Disclosure must be provided as to how the number is calculated from the company's audited financial statements.
- If the Company-Selected Measure or any additional measures that the company elects to provide in the Pay Versus Performance Table are non-GAAP financial measures, they will not be subject to Regulation G and Item 10(e) of Regulation S-K.

Interplay with ESG Performance

- The final rules bucket ESG metrics as nonfinancial performance goals, along with measures of individual performance or broader "strategic goals."
- While the final rules do not require disclosure of ESG metrics, registrants may supplement their mandatory pay-for-performance disclosure with a discussion of ESG metrics (or any other nonfinancial performance measure), consistent with the requirements of Item 402(v)(6)(iii).
- Consider that – like other nonfinancial, goal-oriented metrics – ESG-related goals will require advance planning and thought as to how achievement will be determined and reflected in the disclosure.

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Overview of Final Rule 10D-1

Final Rule 10D-1 directs the national securities exchanges to establish listing standards that require **each issuer** to develop and implement a **required policy** providing for the recovery, in the event of a **required accounting restatement**, of **incentive-based compensation** received by **current or former executive officers** during **the coverage period** where that compensation is based on the erroneously reported **financial information**.

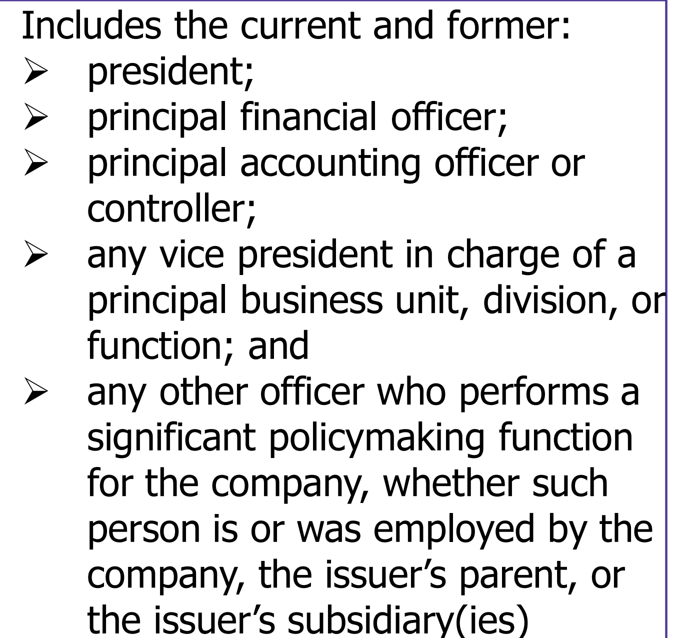
- **Covered Issuers:** broadly applicable to any company listed on a national exchange, including smaller reporting companies (SRCs), emerging growth companies (EGCs), and foreign private issuers (FPIs)
- **Required Clawback Policy:** a written policy to recoup incentive-based compensation in the event of an accounting restatement
- Final Rule applies to covered executives, without regard to whether the covered executive is "at fault"
- The listing standards must mandate recovery (not discretionary)
- Listed companies that do not adopt, disclose, and comply with an applicable exchange's listing standards and the related recovery policies will be subject to delisting from that exchange

Timing and Transition

Action	Timing
Exchanges file proposed listing rules	prior to February 27, 2023 (i.e., within 90 days after publication of the Final Rule)
Exchanges' rules must be effective	prior to November 28, 2023 (i.e., within 1 year after publication of the Final Rule)
Companies must adopt a recovery policy	within 60 days after the effective date of the applicable exchange's rules
Companies must comply with the required clawback policy and recover all excess incentive-based compensation resulting from an accounting restatement	for any compensation received after the effective date of the applicable listing standard
Companies must comply with the new disclosures in proxy or information statements and Exchange Act annual reports	for all filings on or after the effective date of the applicable exchange's rules

Which Executives Are Covered by the Final Rule?

- Rule 10D-1 applies to any current or former **executive officer** of a covered company
  - Relies on the same definition as for Section 16 officers
  - Does not apply only to named executive officers that are the subject of compensation disclosure in the Company's annual proxy statement
- Any person who was an executive officer during the "performance period" is subject to clawback
- It applies to any compensation received after becoming an executive officer



What Is Included in Incentive-Based Compensation?

- Non-equity **incentive plan awards** that are earned based wholly or in part on satisfying a financial reporting measure performance goal
- **Equity awards** (including restricted stock, restricted stock units (RSUs), performance share units, stock options, and stock appreciation rights) that are granted or become vested based wholly or in part on satisfying a financial reporting measure performance goal
- Bonuses paid from a **bonus pool** based wholly or in part on satisfying a financial reporting measure performance goal
- Other **cash bonuses** and other cash-based awards with payment or vesting based on satisfaction of a financial reporting measure performance goal
- **Proceeds** received from the sale of shares acquired through an incentive plan granted or vested based wholly or in part on satisfying a financial reporting measure performance goal
- **Financial reporting measures**, including non-GAAP financial measures
  - Estimates must be reasonable and the company must maintain documentation of the determination of the estimate and provide it to its exchange

What Is **Not** Included in Incentive-Based Compensation?

- Incentive-based compensation **does not include**:
  - Awards that vest *solely* on the basis of completion of a specified employment period, such as service-vesting stock options, restricted stock, or RSUs
  - Awards that are granted, earned, or become vested based solely upon the occurrence of certain non-financial events, for example:
    - Opening a specified number of stores
    - Obtaining regulatory approval for a product
  - Awards earned *solely* upon satisfaction of strategic measures, such as completing a merger, divestiture, or similar transaction
  - Salaries
  - Discretionary bonuses
  - Bonuses paid based on subjective standards, such as leadership

When Is Incentive-Based Compensation Subject to Recovery?

- Incentive-based compensation is deemed to be **received**, and therefore recoverable, in the fiscal period when the financial reporting measure specified in the incentive-based compensation award is attained
- The actual payment date does not matter

Type of Award	When Received
Equity award that vests upon satisfaction of a financial reporting measure and subsequent service	Deemed received in the fiscal period when the financial reporting measure is satisfied
Cash award earned upon satisfaction of a financial reporting measure	Deemed received in the fiscal period when the financial reporting measure is satisfied

➢ Because incentive-based compensation awards may have both service and performance conditions, an incentive award may be deemed to be "received" before payment is made

What Is a Restatement?

- Under the Final Rule, clawback policies must mandate compensation recovery in the event a company is required to prepare an accounting **restatement** due to its material noncompliance with any financial reporting requirement under the securities laws
- The Final Rule applies to both "big R" and "little r" restatements.
- "**Big R**" restatements correct **material** errors to previously issued financial statements and require companies to file an Item 4.02 Form 8-K and amend their filings promptly to restate the previously issued financial statements
- "**Little r**" restatements correct errors that are not material to previously issued financial statements, but would result in a material misstatement if (1) the errors were left uncorrected in the current filing or (2) the error correction was recognized in the current period. As such, this includes any corrections made when filing the prior year's financial statements and generally does not require an Item 4.02 Form 8-K

The inclusion of "little r" restatements is a stark departure from the original 2015 rule proposal

The SEC notes in the adopting release that "both types of restatements address material noncompliance . . . with the financial reporting requirements"

The SEC also conveyed that this expanded approach addresses concerns that companies "could manipulate materiality and restatement determinations to avoid application of the recovery policy"

What Types of Financial Statement Changes Do Not Constitute a Restatement?

- Consistent with the proposed rule, the Final Rule issuing release provides that the following types of changes to an issuer's financial statements **do not represent error corrections** and, therefore, would not trigger application of a clawback policy:
  - Application of a change in accounting principle
  - Revision to reportable segment information due to a change in the structure of an issuer's internal organization
  - Reclassification due to a discontinued operation
  - Application of a change in reporting entity, such as from a reorganization of entities under common control
  - Adjustment to provisional amounts in connection with a prior business combination
  - Revision for stock splits

What Amount of Incentive-Based Compensation Is Recoverable?

- Recoverable compensation = **excess compensation** = amount the executive received less the amount the executive would have received had the incentive-based compensation been based on the accounting restatement
- Recoverable compensation is calculated on a **pre-tax basis**
- Under the Internal Revenue Code, it is generally possible for an executive to recoup the taxes previously paid on recovered/clawed-back compensation, but only through somewhat complicated tax provisions

Are There Any Exceptions to the Final Rule?

- There are three incredibly narrow exceptions to the requirements of the Final Rule:
  1. recovery is **impracticable** due to costs, determined following an initial attempt to collect,
  2. recovery would **violate a home-country law** adopted before the publication of Final Rule 10D-1 (provided such conclusion is based on an opinion of home-country counsel), and
  3. recovery need not extend to any compensation contributed to **tax-qualified plans**
- Any determination must be made by an independent compensation committee
- Note that there is **no de minimis exception**, which the SEC said in its issuing release as carrying the risk that such exemption would be over- and under-inclusive.

Impracticability exception is very limited

The direct expense paid to a third party to assist in enforcing recovery would need to exceed the amount to be recovered

Before reaching the conclusion that recovery is "impracticable," a company must first "make a reasonable attempt to recover" the compensation, document its attempts, and provide the documentation to its exchange

May a Company Provide Indemnification to Executive Officers?

- The Final Rule **prohibits** a listed company from indemnifying or purchasing insurance for any executive officer or former executive officer against the loss of any erroneously awarded compensation
  - The SEC believes that such indemnification arrangements "fundamentally undermine the purpose of Section 10D"
- Executive officers could personally purchase **third-party insurance** (to the extent that such insurance is available) to fund potential recovery obligations
  - Listed companies are not permitted to pay, or reimburse the executive officer for, premiums

Reporting and Disclosure Obligations

New Annual Report Cover Page	**New Annual Report Cover Page** must also disclose by check boxes on the cover page whether the financial statements included in the filings reflect correction of an error and whether such error corrections are restatements that require a recovery analysis
New Disclosure Rules	**New Disclosure Rules** (under Regulation S-K Item 402(w) or applicable forms for issuers who don't rely on Regulation S-K) will require companies to disclose "recovery" policies and actions taken to recover erroneously awarded executive compensation during or following the end of the most recently completed fiscal year, including a requirement to provide: - The date on which the listed issuer was required to prepare an accounting restatement and the aggregate dollar amount of erroneously awarded incentive-based compensation attributable to such accounting restatement; - The aggregate amount of incentive-based compensation that was erroneously awarded to all current and former named executive officers that remains outstanding at the end of the last completed fiscal year; - Any outstanding amounts due from any current or former executive officer for 180 days or more, separately identified for each named executive officer (or, if the amount of such erroneously awarded incentive compensation has not yet been determined as of the time of the report, disclosure of this fact and an explanation of the reasons why); and - If recovery would be impracticable, for each current and former named executive officer and for all other current and former executive officers as a group, the amount of recovery forgone and a brief description of the reason the listed registrant decided in each case not to pursue recovery. - Note that, if an amount is properly determined to be non-recoverable due to impracticality, such amount will not be considered to be outstanding at the last fiscal year for purposes of the disclosure requirements described above

Reporting and Disclosure Obligations (cont.)

New Exhibit Filing	**New Exhibit Filing**: the new rules will require the clawback policy to be filed as an exhibit to the annual report on Form 10-K, 20-F, or 40-F
XBRL	**XBRL:** the new disclosure on the cover page of the Form 10-K, 20-F, or 40-F, as applicable, and Item 402(w) with respect to domestic companies must be tagged in interactive block text tag format using eXtensible Business Reporting Language

What Should Companies Do Now?

Companies are not required to adopt clawback policies until the exchanges amend their listing standards to require adoption of clawback policies

- Plan for 2023 implementation

Ensure that employment agreements, equity plans, deferred compensation plans, and bonus/incentive arrangements contain appropriate provisions to enable implementation of the Dodd-Frank recovery policies.

- Create a contractual link between the incentive compensation and the recovery policy

Companies should review their existing clawback policies to determine what modifications will be needed to comply with the new rules. Potential revisions include:

- Which officers are covered (including former officers)
- The types of compensation covered
- The kinds of restatements that trigger compensation recovery
- The lookback period
- The mandatory nature of clawbacks under the new rules (no discretion; no-fault)
- The limited exceptions to compensation recovery

What Should Companies Do Now? (cont.)

Consider whether to limit the company's policy to the Dodd Frank policy or to add other discretionary clawbacks such as:

- Misconduct/breach of restrictive covenants
- Clawback for broader group of responsible employees if the Dodd Frank clawback is triggered for executive officers

Identify financial measures that may cause incentive compensation to become subject to recovery and consider how the recovery process would work

- This is especially important for stock price and TSR measures

Consider shift toward types of compensation that would not be covered by the clawback rules, such as:

- Equity compensation that vests based on service
- Incentive compensation using non-financial/non-stock price measures
- Discretionary awards

Consider imposing mandatory deferrals or holding requirements on earned incentive awards to facilitate implementation of the recovery policy

Review committee charters and other relevant board documents to ensure that the responsibility for determining the Dodd-Frank recovery process is appropriately addressed

Prepare to devote sufficient time and resources to develop a policy that is both compliant with the final rules and appropriate for the company's compensation policies and governance programs

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ESG: Not Just Environmental

Environmental

- Greenhouse gas emissions
- Climate change
- Energy use
- Water use
- Pollution
- Hazardous waste
- Recycling
- Sustainability
- Deforestation

Social

- Corporate giving and philanthropy
- Working conditions/supply chain
- Workplace health and safety
- Compensation and benefits
- Internal pay equity
- Employee opportunity
- Labor and human rights
- Child and forced labor
- Diversity and inclusion
- Supplier practices

Governance

- Board structure and composition (including tenure and diversity)
- Executive compensation
- Corruption
- Shareholder rights
- Enterprise risk management
- Audit oversight
- Disclosure and reporting
- Ethics and compliance
- Privacy and cybersecurity

ESG Reporting: Why Is It Important?

ESG reporting deals with the public disclosure of data regarding an organization's environmental, social, and corporate governance initiatives and performance

Rise in board and corporate accountability for addressing ESG issues

Increase in ESG due diligence by buyers/investors

Uptick in ESG stockholder proposals and activist campaigns

Enhanced disclosure related to climate change proposed by the US Securities and Exchange Commission (SEC)

Proposed SEC Rules

- On March 21, 2022, the SEC issued a proposed rule that would enhance and standardize climate disclosure requirements provided by public companies
- If adopted, the proposed rule will require public companies to provide certain climate disclosures in registration statements and annual reports, which include:
  i. Oversight and governance of climate-related risk by the board and management
  ii. A process for identifying, assessing, and managing climate-related risks and their impact
  iii. Climate-related financial impact and expenditure metrics
  iv. A discussion of climate-related targets, goals and transition plans
  v. The effects of severe weather events and related natural conditions
  vi. Assumptions in the financial statements

Disclosure of Scopes 1, 2, and 3

The SEC's proposal also requires the disclosure of certain greenhouse gas (GHG) emissions. These emissions are divided into three categories:

Scope 1	Scope 2	Scope 3
"What you burn" Scope 1 emissions are direct GHG emissions that occur from sources that are controlled or owned by an organization (e.g., emissions associated with fuel combustion in boilers, furnaces, vehicles)	**"What you buy"** Scope 2 emissions are indirect GHG emissions associated with the purchase of electricity, steam, heat, or cooling	**"Everything else"** Scope 3 emissions are the result of activities from assets not owned or controlled by the reporting organization and include all sources not within an organization's Scope 1 and Scope 2 parameters ➢ The Scope 3 emissions for one organization are the Scope 1 and 2 emissions of another organization (e.g., a supplier) ➢ Scope 3 emissions, also referred to as value chain emissions, often represent most of an organization's total GHG emissions

Best Practices

1

Provide disclosure on ESG risk management and board oversight of ESG

2

Maintain consistency and accuracy in disclosing climate-related information

- Have support for statements
- Confirm that information across all media and filings is uniform and consistent

3

Be mindful that SEC review and scrutiny goes beyond ESG disclosure in SEC filings, and could include:

- Company websites
- Press releases
- Marketing materials
- Blogs
- CSR/sustainability reports

Best Practices (cont.)

4 **Carefully consider inadvertent incorporation by reference**

5 **Third-party verification or audit**

- Conduct internal audits

6 **Avoid "commitment" language**

- Statements that the company will achieve a goal threshold by a given date

7 **If appropriate, use forward-looking statements and provide appropriate disclaimers**

Linking Executive Compensation to ESG Performance

- A new survey from The Conference Board indicates that linking executive comp to ESG principles is used by the "vast majority" of S&P 500 companies
  - From 66% in 2021 to 73% in 2022
  - The most common approach is use of diversity, equity, and inclusion-related goals, which rose from 35% in 2020 to 51% in 2021
  - S&P 500 companies that tied carbon footprint and emissions reduction goals to executive pay grew from 10% in 2020 to 19% in 2021
- Differing approaches are used to factor ESG into executive pay
  - Modifier to the overall performance rating (6%)
  - Stand-alone specific metrics (24%)
  - Include ESG goals as part of a broader business strategy scorecard (48%)
  - Include as part of an executive's individual performance rating (49%)

Linking Executive Compensation to ESG Performance (cont.)

- Primary reasons companies incorporate ESG measures into executive comp:
  - To signal that ESG is a priority
  - To respond to investor expectations
  - To help achieve the ESG commitments the company has made
- Cautions regarding the incorporation of ESG measures into executive comp:
  - Consider using ESG goals for one or two years before including them in comp programs to allow time to see if the goals are relevant and to obtain management buy-in
  - Developing and compiling reliable, meaningful data used to measure and report company performance against ESG goals can be challenging
  - ESG incentive models should be tailored to a company's specific situation
  - Companies will need to explain why including ESG goals as part of their exec comp program makes business sense and will move the needle on the company's performance
  - Measuring the impact of ESG performance goals in compensation is more challenging than measuring the impact of traditional performance metrics

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Key Changes at a Glance

- Updated voting policies primarily concern:
  - Director diversity and overboarding
  - Board oversight of environmental and social issues
  - Oversight of cyber-related risks
  - Board accountability, including for climate-related issues
- Updated Glass Lewis proxy voting guidelines are **now in effect** for shareholder meetings held on or after **January 1, 2023**
- Updated ISS voting policies **will go into effect** for shareholder meetings held on or after **February 1, 2023**

ISS: Board Composition/Diversity

Board gender diversity will be expanded from Russell 3000 and S&P 1500 companies to all US companies

For companies without women on the board, ISS will generally recommend voting against the chair of the nominating committee

- An exception will be made if there was at least one woman on the board at the preceding annual meeting and the board makes a firm commitment to returning to a gender-diverse status within a year

Glass Lewis: Board Composition/Diversity

Approach continues to transition from a fixed numerical to a percentage-based approach, recommending that the board of companies within the Russell 3000 index be at least 30% gender diverse

- If the 30% threshold is not met, Glass Lewis will generally recommend voting against the chair of the nominating committee of the board, but may refrain from doing so when the board has provided sufficient rationale or a plan to address the lack of gender diversity, including a timeline to appoint additional gender diverse directors

Starting in 2023, Glass Lewis will generally recommend voting against the nominating committee chair at Russell 1000 companies with no directors from under-represented communities on the board

- Glass Lewis will rely on self-identified demographic information disclosed in company proxy statements for purposes of this evaluation

Glass Lewis: Board Composition/Diversity (cont.)

During 2023, Glass Lewis will refrain from providing recommendations regarding board composition in compliance with California's Senate Bill 826 and Assembly Bill 979

- These laws have been challenged and are in the appeals process

In 2023, Glass Lewis will generally recommend voting against the chair of the nominating/governance committee at Russell 1000 index companies that have not provided any disclosure of individual or aggregate racial/ethnic minority demographic information for directors

- Additionally, Glass Lewis will generally recommend voting against the chair of the nominating and/or governance committee of a Russell 1000 index company that fails to provide any disclosure in the director diversity and skills categories tracked by Glass Lewis

Glass Lewis: Board Oversight of Cyber Risk

- Glass Lewis encourages all issuers to provide clear disclosures surrounding the role of the board in overseeing cybersecurity-related issues
  - Additionally, disclosure explaining how companies ensure that directors understand major security issues can help shareholders understand the seriousness with which companies handle this issue
  - Glass Lewis generally will not generally make recommendations based on a company's oversight or disclosure concerning cyber-related issues – but will evaluate disclosure when a material cyber-attack has occurred

Glass Lewis: Board Oversight of Environmental and Social Issues

- Glass Lewis will generally recommend voting against the governance committee chairs of Russell 1000 index companies that fail to provide explicit disclosures about the board's role in overseeing environmental and social issues
  - Additionally, Glass Lewis will expand its tracking of this board-level oversight to all companies within the Russell 3000 index
- Glass Lewis believes that companies should individually determine the best structure for this oversight
  - Oversight can be conducted by specific directors, the entire board, a separate committee, or combined with the responsibilities of a key committee

Board Accountability for Climate-Related Issues

ISS	Glass Lewis
• ISS will recommend voting against or withholding votes from the chair of the responsible committee (or other directors on a case-by-case basis) where it determines that a high emitting company is not taking "minimum steps" needed to understand, assess, and mitigate risks to the company and economy related to climate change • Minimum steps are: i. detailed climate risk disclosure information, including under the Task Force on Climate-related Financial Disclosures (TCFD), and ii. appropriate GHG emission reduction targets, which are either medium-term GHG reduction targets or "Net Zero-by-2050" GHG emission-reduction targets for at least the company's operations (Scope 1) and electricity use (Scope 2), with such targets covering the vast majority (95%) of direct emissions	• Glass Lewis expects that companies with material exposure to climate risk stemming from their own operations should provide thorough disclosures aligned with the recommendations of the TCFD, and that boards of such companies should have explicit and clearly defined oversight responsibility for climate-related issues • In cases where either disclosure or oversight is absent or significantly lacking, Glass Lewis will recommend that shareholders vote against responsible directors

ISS: Political Expenditures and Lobbying Congruency Shareholder Proposals

- ISS will evaluate proposals requesting more fulsome disclosure of a company's alignment of political contributions, lobbying efforts, and electioneering spending with a company's publicly stated values and policies on a case-by-case basis, considering the following:
  1. the company's policies and level of disclosure related to direct political contributions or contributions to groups that may be used for political purposes;
  2. the company's disclosure regarding the reasons for its support of candidates for public offices; the reasons for its support of and participation in trade associations or other groups that may make political contributions; and other political activities;

ISS: Political Expenditures and Lobbying Congruency Shareholder Proposals (cont.)

iii. any incongruencies between a company's political expenditures and its publicly stated values; and

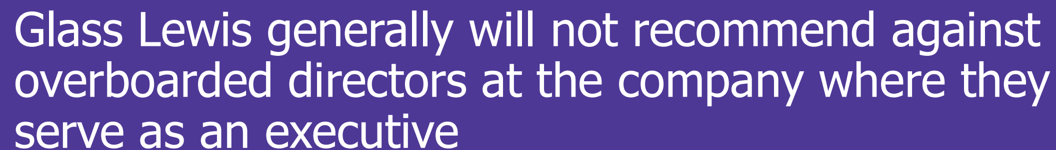
iv. any recent significant controversies related to the company's lobbying, political contributions, or political activities

- Additionally, ISS will evaluate proposals requesting comparison of a company's political spending to objectives that can mitigate material risks for the company

Glass Lewis: Director Commitments and Overboarding

Glass Lewis will generally recommend that shareholders vote against:

- a director who serves as an executive officer (except as executive chair) of any public company while serving on more than one external public company board;
- a director who serves as an executive chair of any public company while serving on more than two external public company boards; and
- any other director who serves on more than five public company boards



ISS: Board Accountability for Problematic Governance Structures

- Starting on **February 1, 2023**, ISS will recommend voting against directors at all companies with unequal voting rights structures, not just newly-public companies
- Exceptions:
  - Newly public companies with a sunset provision of no more than 7 years from the date the company went public
  - Limited partnerships
  - Super-voting shares represent less than 5% of total voting power
  - Sufficient protections provided for minority shareholders

Officer Exculpation Provisions in Charter

Delaware corporations now have the option to adopts in certificates of incorporation eliminating or limiting monetary liability of certain officers for breach of fiduciary duty of care

ISS

- ISS will generally evaluate proposals to add officer exculpation provisions to a company's charter on a case-by-case basis, considering the stated rationale for the proposal

Glass Lewis

- Glass Lewis will evaluate proposals to adopt such exculpation provisions on a case-by-case basis
- However, Glass Lewis will recommend that shareholders vote against such proposals, unless a compelling rationale for the adoption is provided by the board and the provisions are reasonable

ISS: Other Governance Updates

Poison Pills: ISS has clarified its policy to provide that the ownership level at which the pill is triggered (i.e., low trigger thresholds of 5%-10%) is also a consideration in evaluating the appropriateness of the board's actions in adopting a short-term pill that is not put to a shareholder vote

Unilateral Board Actions: ISS has clarified its policy to explicitly provide that fee-shifting provisions unilaterally adopted by the board are considered an ongoing governance failure that will generally result in "against" recommendations in director elections, as will the unilateral adoption of provisions that ISS deems "egregious"

Glass Lewis and ISS Executive Compensation Updates

- Glass Lewis
  - Increased the minimum percentage of long-term incentive grants that should be performance based from 33% to 50%
    - Will raise concerns with executive pay programs that provide less than 50% of an executive's incentive award subject to performance-vesting
  - Clarified that Glass Lewis will vote against compensation committee chairs if there are mega-grants which present concern (e.g., excessive amount, lack of sufficient performance conditions, excessively dilutive)
  - Fleshed out policies/concerns regarding front-loaded awards
- ISS
  - Problematic Pay Practice Clarifications
    - Clarifies that the enumerated list in guidance provides examples and is not exhaustive
      - Enumerated items include: repricing underwater options/SARs without shareholder approval, extraordinary perks or tax gross-ups, and liberal CIC definition combined with single-trigger CIC payments
    - Specifically adds to the enumerated list: severance payments made when termination is not clearly disclosed as involuntary
      - Codifies ISS' current approach to evaluating severance payments when the termination is not clearly disclosed as involuntary

ISS: Equity Plan Scorecard Updates

- ISS considers the following three “pillars” in assessing omnibus equity plans:
  - 45 Points: Plan cost (i.e., dilution and overhang)
  - 38 Points: Grant practices (i.e., burn rate relative to peer companies, CEO vesting terms)
  - 17 Points: Plan features (e.g., minimum vesting periods, extent to which vesting can be accelerated on a discretionary basis, liberal share recycling, change-in-control provisions, dividends paid on unvested awards)

ISS: Equity Plan Scorecard

- For the 2023 proxy season
  - Threshold passing score has again been increased
    - from 57 to 59 points for S&P 500 model
    - from 55 to 57 points for Russell 3000 model
    - from 53 to 55 points for Non-Russell 3000 model
  - There are no changes to the pillars or weightings
  - "Value Adjusted Burn Rate" now in effect and replaces the prior burn rate factor
    - is intended to use more accurate measures for the value of equity-based awards
- Clawbacks
  - To receive points, the company's clawback policy should authorize recovery upon a financial restatement and cover all or most equity-based compensation for all NEOs (including time and performance vesting equity awards)

Our Global Reach

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Asia Pacific
Europe
Latin America
Middle East
North America

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Frankfurt
Hartford
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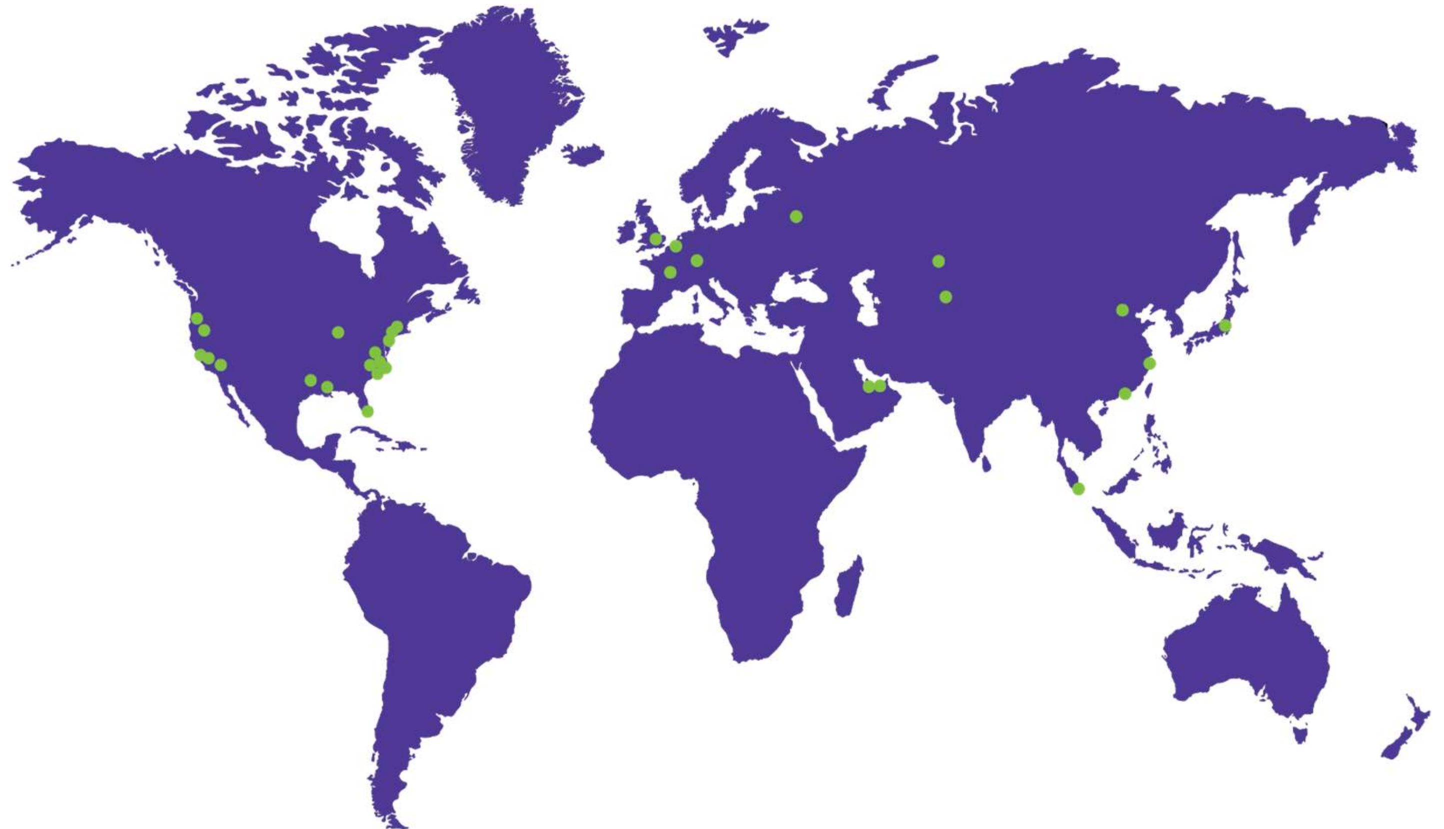
Wilmington



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