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ISS and Glass Lewis Policy Updates for 2023

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Securities and Capital Markets

Both Institutional Shareholder Services Inc. ("ISS") and Glass Lewis have announced updates to their voting guidelines for the 2023 proxy season. Changes to ISS's benchmark voting policies will apply for shareholder meetings to be held on or after February 1, 2023, and updates to Glass Lewis's proxy voting guidance will apply for shareholder meetings to be held on or after January 1, 2023.

The updates primarily concern director diversity and commitments, board oversight of environmental and social issues and cyber-related risks, and board accountability, including for climate-related issues. Additionally, Glass Lewis published its 2023 Environmental, Social & Governance (ESG) Initiatives Policy Guidelines, addressing ESG-related shareholder proposals.

I. Summary of Key Changes

The table below summarizes the most notable updates to the guidelines. These are discussed in more detail in the section following the table.

Topic	ISS	Glass Lewis
Board Composition/Diversity	Recommend *against* the chair of the nominating committee if a board does not have at least one female director. For 2023, this policy is extended to all companies.	Recommend *against* the chair of the nominating committee if a board is not at least 30% gender diverse (Russell 3000 companies) or has no directors from an underrepresented community (Russell 1000 companies). Recommend *against* the chair of the governance committee at Russell 1000 companies that have not provided any disclosure of racial/ethnic minority demographic information for directors.
Board Oversight of Cyber Risk	No changes.	Encourages all companies to provide clear disclosures surrounding the role of the board in overseeing cybersecurity-related issues. May recommend *against* directors in specific instances where cyber-attacks have caused harm to shareholders and oversight was insufficient.
Board Oversight of Environmental and Social Issues	No changes.	Recommend *against* the chair of the governance committee at Russell 1000 companies that fail to provide explicit disclosures about the board's role in overseeing environmental and social issues.

Environmental and Social Shareholder Proposals	Generally vote case-by-case on shareholder proposals (i) requesting greater disclosure of a company's alignment of political contributions, lobbying, and electioneering spending with a company's publicly stated values and policies and (ii) requesting a comparison of a company's political spending to objectives that can mitigate material risks for the company such as limiting global warming.	No changes.
Director Commitments and Overboarding	No changes.	Clarified the thresholds for the number of external boards on which a director may sit before being considered overboarded, including for directors who serve as executive officers or executive chairs at other public companies.
Board Accountability for Climate-Related Issues	For certain high emitting companies that lack appropriate climate risk disclosure and greenhouse gas reduction targets, recommend *against* appropriate directors.	For companies with material exposure to climate risk stemming from their own operations that lack appropriate climate risk disclosures or do not have clearly defined board oversight responsibilities, recommend *against* responsible directors.
Board Accountability for Problematic Governance Structures	Recommend *against* directors at all companies (not just newly public companies) with unequal voting right structures (subject to certain exceptions including for newly public companies with a sunset provision of 7 years or less and where super-voting shares are less than 5% of total voting power).	No changes.
Officer Exculpation Provisions in Charter	Generally consider on case-by-case basis, considering the stated rationale for the proposal.	Generally recommend *against*, unless the provision is reasonable and the board provides a compelling rationale for adoption.
Long-Term Incentive Awards	No changes.	Increased the recommended minimum percentage of a long-term incentive grant that should be performance-based from 33% to 50%.
Poison Pills	For short-term pills without shareholder approval, will now also consider the trigger threshold and the company's market capitalization in evaluating the appropriateness of the board's actions.	No changes.

II. Key ISS and Glass Lewis Guideline Changes

A. Board Composition/Diversity

- *Gender diversity*: For shareholder meetings on or after February 1, 2023, **ISS**'s policy on board gender diversity will be expanded from Russell 3000 and S&P1500 companies to all U.S. companies. For companies without any women on the board, ISS will generally recommend 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 return to a gender-diverse status within a year.

  Glass Lewis's board gender diversity approach continues to transition from a fixed numerical to a percentage-based approach, recommending that the boards of companies within the Russell 3000 index be at least 30 percent gender diverse. For companies outside this index, Glass Lewis's current policy requiring at least one gender diverse director remains unchanged. When the 30 percent threshold is not met, Glass Lewis will generally recommend 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.
- *Underrepresented community diversity*: Beginning in 2023, **Glass Lewis** will generally recommend against the chair of the nominating committee of boards of companies within the Russell 1000 index with no directors from an underrepresented community (subject to the same exception as in the case of insufficient gender diversity).
- *California laws on diversity*: During 2023, **Glass Lewis** will refrain from providing recommendations regarding state board composition requirements in California's Senate Bill 826 and Assembly Bill 979, as these laws have been challenged and are in the appeals process.
- *Disclosure of director diversity*: In 2023, **Glass Lewis** will generally recommend voting against the chair of the 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, it will generally recommend voting against the chair of the nominating and/or governance committee where a Russell 1000 index company fails to provide any disclosures in each of the director diversity and skills categories tracked by Glass Lewis.

B. Board Oversight of Cyber Risk:

Recognizing that cyber risk is material for all companies, **Glass Lewis** encourages all issuers to provide clear disclosures surrounding the role of the board in overseeing cybersecurity-related issues. Additionally, Glass Lewis stated that a disclosure explaining how companies ensure that directors understand cyber security issues can help shareholders understand the seriousness with which companies treat this issue.

Glass Lewis will for now not make recommendations on the basis of a company's oversight or disclosure concerning cyber-related issues, but will closely evaluate a company's disclosure in cases where cyber-attacks have caused significant harm to shareholders. If Glass Lewis finds that the disclosure or oversight was insufficient, Glass Lewis may recommend that the shareholders vote against appropriate directors.

C. Board Oversight of Environmental and Social Issues:

Starting in 2023, **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, in 2023 Glass Lewis will expand its tracking of this board-level oversight to all companies within the Russell 3000 index. Glass Lewis highlighted its belief that companies should individually determine the best structure for this oversight, and that such oversight can be effectively conducted by specific directors, the entire board, a separate committee, or combined with the responsibilities of a key committee.

D. Environmental and Social Shareholder Proposals:

ISS has noted an increase in the number of shareholder proposals requesting company transparency on the congruency of its political contributions to its public commitments and/or of its climate lobbying to its climate goals. Starting with shareholder meetings on or after February 1, 2023, ISS will evaluate proposals requesting greater disclosure of a company's alignment of political contributions, lobbying and electioneering spending with a company's publicly stated values and policies on a case-by-case basis, taking into account the following considerations: (i) the company's policies, management, board oversight, governance processes, and level of disclosure related to direct political contributions, lobbying activities, and payments to trade associations, political action committees, or other groups that may be used for political purposes; (ii) the company's disclosure regarding: the reasons for its support of candidates for public offices; the reasons for support of and participation in trade associations or other groups that may make political contributions; and other political activities; (iii) any incongruencies identified between a company's direct and indirect political expenditures and its publicly stated values and priorities; and (iv) any recent significant controversies related to the company's direct and indirect lobbying, political contributions, or political activities.

In addition, **ISS** will evaluate proposals requesting comparison of a company's political spending to objectives that can mitigate material risks for the company, such as limiting global warming, on a case-by-case basis

E. Director Commitments and Overboarding:

Glass Lewis will generally recommend that shareholders vote against (i) 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, (ii) a director who serves as an executive chair of any public company while serving on more than two external public company boards, and (iii) any other director who serves on more than five public company boards.

F. Board Accountability for Climate-Related Issues:

Both ISS and Glass Lewis issued updates to their previously-announced policies on board accountability for climate-related issues.

For shareholder meetings on or after February 1, 2023, **ISS** will recommend voting against or withhold from the incumbent chair of the responsible committee (or other directors on a case-by-case basis) where it determines that a high emitting company (identified as those in the Climate Action 100+ Focus Group) is not taking certain minimum steps needed to understand, assess, and mitigate risks related to climate change to the company and the larger economy. The following minimum steps will be considered: (i) detailed climate risk disclosure information, including under the Task Force on Climate-related Financial Disclosures ("TCFD"), and (ii) appropriate greenhouse gas ("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 believes that companies with material exposure to climate risk stemming from their own operations should provide to shareholders thorough disclosures aligned with the recommendations of the TCFD, and boards of such companies should have explicit and clearly defined oversight responsibilities over climate-related issues. In cases where either the disclosures or the clearly defined oversight are absent or significantly lacking, Glass Lewis will recommend shareholders vote against responsible directors.

G. Board Accountability for Problematic Governance Structures:

The one-year transition period delaying **ISS**'s adverse voting recommendations for companies with capital structures having unequal voting rights will end, and beginning with shareholder meetings on or after

February 1, 2023, ISS will recommend against directors at all companies with unequal voting right structures, not just newly-public companies. This policy is subject to certain exceptions, including for newly public companies with a sunset provision of no more than 7 years from the date the company went public, and where the super-voting shares represent less than 5 percent of total voting power.

Additionally, under its current guidelines, **ISS** will recommend against directors at companies that go public with problematic governance structures that are considered materially adverse to shareholder rights (including classified boards, supermajority vote requirements and other egregious provisions), but will consider a reasonable sunset provision for phasing out such structures as a mitigating factor. Beginning with shareholder meetings on or after February 1, 2023, ISS will define this “reasonable sunset period” for the phase out of such structures to be no more than 7 years from the date the company went public.

H. Officer Exculpation Provisions in Charter:

As a result of an amendment to the Delaware General Corporation Law in 2022, a Delaware corporation now has the option to adopt a provision in its certificate of incorporation eliminating or limiting monetary liability of certain officers for breach of their fiduciary duty of care.

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

Glass Lewis will evaluate proposals to adopt such exculpation provisions on a case-by-case basis. Generally, however, Glass Lewis will recommend shareholders vote against such proposals unless the provision is reasonable and the board provides a compelling rationale for its adoption.

I. Long-term Incentive Awards:

To reflect market trends, **Glass Lewis** revised its recommendation that the minimum percentage of a long-term incentive grant that should be performance-based is 50 percent, rather than the previous 33 percent. While Glass Lewis may refrain from issuing a negative recommendation for executive pay programs that do not follow this recommendation in the absence of other related issues, they will raise their concerns, and eventually may issue an unfavorable recommendation if they observe a negative trajectory in the allocation amount.

J. Poison Pills:

ISS revised its policy regarding poison pills to clarify that, for short-term pills (i.e., those with a term of one year or less) adopted without shareholder approval, ISS will include, in the factors it considers to evaluate the appropriateness of the board’s action, the share ownership trigger threshold and the company’s market capitalization (including absolute level and sudden changes). Under current ISS guidelines, ISS evaluates short term pills on a case-by-case basis taking into account the disclosed rational for the adoption and other factors as relevant, such as a commitment to put any renewal to a shareholder vote. If ISS determines a pill is inappropriate, it will generally recommend against or withhold from all board nominees.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our Securities and Capital Markets practice:

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