Published on *The National Law Review* https://natlawreview.com

Glass Lewis and ISS Announce Updates For 2024 Proxy Season

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Glass Lewis ("GL") recently released its annual Benchmark Policy Guidelines for 2024. This update makes several changes to how the proxy advisory firm will evaluate company policies related to executive compensation. Institutional Shareholder Services ("ISS") also released updates to its voting policies for 2024, including new and updated responses to its Compensation Policies FAQ.

GLASS LEWIS POLICY GUIDELINES UPDATE

Implementation of Clawback Policies. Although publicly traded companies adopted Dodd-Frank clawback policies in light of new NYSE and Nasdaq listing requirements that took effect on December 1, 2023 (discussed in greater detail here), GL's guidelines go beyond the Dodd-Frank requirements relating to material financial restatements, by recommending the adoption of expansive clawback policies that apply to 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. The guidelines also recommend disclosing a company's rationale if it determines to refrain from recouping compensation and alternative measures that are pursued.

Executive Ownership Guidelines. GL outlined the importance of assuring shareholders that executives are acting in their best long-term interests. To further that end, GL introduced a new policy recommending that companies clearly disclose their executive ownership requirements and how the various types of outstanding equity awards are counted or excluded from the ownership level calculation.

Equity Awards for Shareholders. With respect to individual equity awards granted to large shareholders, GL highlighted the potential conflict of interest when large shareholders are permitted to vote on equity awards for themselves. GL recommended that companies require an abstention vote or non-vote from the recipient for an equity award proposal when the shareholder's vote can materially affect the proposal's passage.

Pay-Versus-Performance Disclosure. The guidelines note that GL may use the SEC-mandated pay-versus-performance disclosure in its pay-for-performance grade supplemental quantitative assessments.

Response to Say-on-Pay Opposition. GL clarified that it considers votes cast as either against and/or abstain as opposition to a say-on-pay vote.

ISS COMPENSATION POLICIES FAQ UPDATE

Changes to Pay-for-Performance Screens. Although there are no changes to the primary pay for performance screens (Relative Degree of Alignment, Multiple of Median, and Pay-Total Shareholder Return Alignment), ISS announced slight changes to the secondary screen Financial Performance Assessment's ("FPA") "eligible for FPA Adjustment" annual threshold and noted that FPA may modify an Overall Quantitative Concern level from a Low to Medium (or vice-versa), or from a Medium to High (or vice versa), depending on the results of the three primary screens and the company's FPA result.

Remedial Action. ISS clarified that although it may issue a "proxy alert" to update its analysis and, if warranted, change a vote recommendation in light of sufficient remedial action, ISS will generally not change vote recommendations if the additional public filing is made in close proximity to the meeting date (specifically, less than five business days before the meeting date). In addition, to change a vote recommendation, the disclosure should be specific as to what changes were made to mitigate ISS's concerns.

Non-GAAP Metrics in Incentive Pay Programs. Non-GAAP metrics utilized in incentive pay programs can be significantly changed by adjustments approved by the board. ISS added a FAQ stating that if such adjustments materially increase incentive payouts, companies should provide clear disclosure in the proxy explaining the nature of the adjustment, its impact (dollar or percentage) on payouts, and the board's rationale and disclosure in the proxy of line-item reconciliation to GAAP results, when possible, is considered a best practice. The absence of these disclosures would be viewed negatively, as would adjustments that appear to insulate executives from performance failures.

Problematic Change-In-Control Severance Arrangements. ISS clarified its standards for reviewing new or materially amended executive agreements that provide for change-in-control severance without requiring a qualifying termination, which ISS considers to be a problematic pay practice. Specifically, ISS distinguished single or modified single trigger change-in-control severance awards from bona fide incentive awards that become payable upon a change-in-control transaction. With respect to new or materially amended executive agreements, ISS will make the distinction between these problematic severance arrangements and bona fide incentive awards by examining the company's disclosure of the incentive award structure and award rationale and whether separate non-problematic severance entitlements are in place. ISS highlighted this difference with the example that if an agreement provides a change-in-control transaction bonus linked to an acquisition premium, such a bonus would be analyzed as a change-in-control incentive award, not as problematic severance. ISS cautioned, however, that change-in-control incentive awards are still evaluated qualitatively, and issues such as excessive magnitude or unclear rationale may raise concerns from a pay-for-performance perspective.

LOOKING FORWARD

GL began applying its new guidelines January 1, 2024, and the ISS updates are effective February 1, 2024.

National Law Review, Volume XIV, Number 9

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