

November 18, 2019

ISS and Glass Lewis Update Their Proxy Voting Guidelines for the 2020 Proxy Season

Institutional Shareholder Services Inc. (ISS) and Glass, Lewis & Co. (Glass Lewis) have both released updates to their proxy voting guidelines.¹ This Alert briefly summarizes the more significant changes to each firm's policies for the 2020 proxy season. Overall, these policy changes represent relatively modest updates from last year and appear to reflect the social and governance concerns of many institutional investors. Companies should review and consider the applicability of the new proxy voting guidelines in light of their individual situations.

ISS's revised policies will apply to annual meetings held on or after February 1, 2020, while Glass Lewis's revised policies will generally apply to meetings held on or after January 1, 2020.

Key Updates to ISS's Proxy Voting Guidelines

Board Gender Diversity

ISS's updated policy on board gender diversity provides that it will generally issue adverse voting recommendations against nominating committee chairs (and other directors on a case-by-case basis) at companies in either the Russell 3000 or S&P 1500 indices where there are no women directors. This updated policy will be in effect for the 2020 proxy season. In addition, ISS clarified that, for companies with no women directors, a firm commitment to appoint one will only be a mitigating factor for 2020 but not for subsequent years.

Problematic Governance Structures at Newly-Public Companies

ISS cited the increasing prevalence of multi-class capital structures with disparate voting rights among newly-public companies as the main rationale for revising its policy approach for newly-public companies by creating two separate policies that address (i) multi-class capital structures with unequal voting rights, and (ii) other problematic governance provisions.

Under the first policy, ISS will generally issue adverse voting recommendations against the entire board (except new nominees, who will be considered on a case-by-case basis) if, prior to or in connection with the company's IPO, the company adopted a multi-class capital structure with unequal voting rights without a reasonable, time-based sunset provision of no more than seven years. ISS will continue to issue adverse voting recommendations against incumbent directors in subsequent years, unless the problematic capital structure is reversed or removed. In assessing the reasonableness of a time-based sunset provision, ISS will consider the company's lifespan, its post-IPO ownership structure and the board's disclosed rationale for the selected sunset period. No sunset period greater than seven years from the date of the IPO will be considered to be reasonable.

ISS clarified and narrowed the focus of the second policy to certain "highly problematic" governance structures, such as supermajority vote requirements to amend a company's charter or bylaws, a classified board structure and other "egregious" provisions. This policy also provides that a reasonable sunset provision will be considered a mitigating factor.

¹ ISS, [Executive Summary of ISS Benchmark Policy Updates](#) (Nov. 12, 2019) and [Americas Proxy Voting Guidelines – Updates for 2020](#) (Nov. 12, 2019); Glass Lewis, [2020 Proxy Paper Guidelines: An Overview of the Glass Lewis Approach to Proxy Advice – United States](#) (Nov. 4, 2019) and [2020 Proxy Paper Guidelines: An Overview of the Glass Lewis Approach to Proxy Advice – Shareholder Initiatives](#) (Nov. 4, 2019).

Share Repurchase Programs

ISS generally recommends in favor of management-sponsored share buyback proposals absent company-specific concerns. ISS updated its delineation of those concerns by identifying greenmail, manipulation of incentive compensation metrics and buybacks that threaten a company's long-term viability. Unlike most of ISS's capital-related policies (which are based on a company's country of incorporation), this ISS policy will cover foreign-incorporated domestic issuers that are listed on a U.S. stock exchange. The policy recognizes that most U.S. companies implement share buyback programs without shareholder approval.

Rule 14a-8 No-Action Requests

As we described in this prior [Alert](#), the SEC's Division of Corporation Finance recently announced that it would not necessarily respond to all Rule 14a-8 no-action requests, either in writing or at all. The staff's response to a request for no-action relief could be that the staff concurs, disagrees or declines to state a view with respect to a company's asserted basis for exclusion. In addition, beginning in the 2019-20 proxy season, the staff may respond to some requests orally, instead of in writing.

Unlike Glass Lewis (as discussed below), ISS's latest policy updates do not directly address the SEC staff's new procedures for handling Rule 14a-8 no-action requests. It is worth noting that, before the staff's announcement, ISS's governance failures policy provided that it would generally recommend a vote against one or more directors (based on case-specific facts and circumstances) if a company omitted a shareholder proposal from its proxy materials when it had not obtained: (i) voluntary withdrawal of the proposal by the proponent, (ii) no-action relief from the SEC, or (iii) a U.S. District Court ruling that it can exclude the proposal.

Shareholder Proposals

Independent Board Chair. ISS has revised its policy to specifically identify the factors that will generally result in an ISS recommendation in support of an independent board chair proposal, which largely codifies ISS's existing practice.

Pay Gap Reporting. ISS has added "race or ethnicity" to its existing policy on shareholder proposals requesting a report on a company's pay data by gender or a report on a company's policies and goals to reduce any gender pay gap. ISS's policy remains to generally make recommendations on pay gap proposals on a case-by-case basis.

Compensation-Related Policies

U.S. Equity Plan Scorecard (EPSC). In its policy updates, ISS cited the significant decline in the number of companies submitting their equity plans for shareholder approval after the Section 162(m) performance-based compensation exception was repealed by the Tax Cuts and Jobs Act of 2017. As a result, ISS will include the presence of an evergreen feature in an equity plan as an "overriding factor" in its EPSC, which may result in a negative recommendation on an equity plan proposal, regardless of its EPSC score. ISS explained its belief that the presence of evergreen provisions in equity plans "circumvent[s] regular shareholder reapproval of such plans within reasonable time intervals" and "may perpetuate plans with shareholder-unfriendly features."

Economic Value Added (EVA) Data. During the 2019 proxy season, ISS began including EVA metrics in its proxy research reports for informational purposes only. For the 2020 proxy season, ISS plans to incorporate EVA metrics as a secondary financial performance assessment screen in its pay-for-performance model. More details regarding this change will be available in a white paper, which ISS expects to publish in December 2019.

Non-Employee Director Pay. ISS's policy on excessive levels of non-employee director compensation was first introduced for the 2018 proxy season. However, since a negative recommendation from ISS would be triggered only after a recurring **pattern** of excessive non-employee director compensation (i.e., for companies where ISS has identified excessive pay without compelling rationale in two or more consecutive years), the 2020 proxy season will be the first proxy season during which ISS may potentially issue a negative recommendation under this policy.

Additional ISS Policy Updates

In addition to the key policy updates summarized above, ISS is expected to release a complete set of updated policies and FAQs (including related to U.S. compensation policies) before year-end and updated proxy voting guidelines for shareholder proposals at U.S. listed companies in January 2020.

Key Updates to Glass Lewis's Proxy Voting Guidelines

Exclusive Forum

While Glass Lewis typically recommends voting against the governance committee chair where a company has adopted an exclusive forum provision without shareholder approval, Glass Lewis has clarified its policy to make exceptions where the exclusive forum provision is narrowly crafted to suit the company's unique circumstances or includes a reasonable sunset provision.

Nominating and Governance Committee

Glass Lewis has codified additional factors that it will consider when evaluating the performance of governance committee members.

Excluded Shareholder Proposals. Glass Lewis believes that companies should only omit proposals in cases where the SEC staff has explicitly concurred with the company's asserted basis for exclusion. As a result, Glass Lewis has adopted a new policy whereby it will generally recommend voting against all members of the governance committee in cases where the SEC staff has **declined to state a view** on a company's no-action request and the company excludes that shareholder proposal from its proxy materials.

Where the SEC staff has **orally responded** to a company's no-action request and there is "no written record provided by the SEC," Glass Lewis expects the company to provide some disclosure concerning this no-action relief in its proxy statement. In cases where a company has excluded a proposal from its proxy materials without including such disclosure, Glass Lewis will generally recommend against all members of the governance committee. After Glass Lewis issued its policy updates, the SEC staff announced that it would be posting a chart on its website showing its disposition of all no-action requests (as discussed in this [Alert](#)). This chart should satisfy Glass Lewis' "written record" requirement, although it has not yet publicly commented on the staff's announcement.

Board Attendance. Glass Lewis will generally recommend voting against the governance committee chair when directors' records for board and committee meeting attendance are either not disclosed or if the disclosure about a director's attendance at less than 75% of board and committee meetings is vague. This policy update is an important reminder that, where applicable, companies should consider proxy statement disclosure that also explains the reasons for any director's poor attendance.

Compensation Committee

Company Responsiveness to Low Say-on-Pay Vote. Glass Lewis has expanded its discussion of what it considers to be an appropriate response following low shareholder support for a company's say-on-pay proposal (i.e., 80% or less),

including differing levels of responsiveness depending on the severity and persistence of shareholder opposition. Glass Lewis expects robust disclosure of the company's shareholder engagement activities and specific changes made to the compensation program in response to shareholder feedback. Absent such disclosure, Glass Lewis may recommend voting against all members of the compensation committee.

Say-on-Pay Frequency. Glass Lewis has updated its compensation committee performance policy and will generally recommend voting against all members of the compensation committee when the board adopts a frequency for its say-on-pay vote other than the frequency approved by a plurality of the company's shareholders.

Shareholder Proposals

Supermajority Voting. Glass Lewis has codified its policy concerning shareholder proposals requesting that companies eliminate their supermajority voting provisions. In instances where shareholder proposals seeking to eliminate supermajority voting provisions are submitted at controlled companies, Glass Lewis may recommend that shareholders vote against such proposals. Glass Lewis believes that, in these instances, supermajority vote provisions may act to protect minority shareholders and thus should be maintained.

Gender Pay Equity. With respect to gender pay gap shareholder proposals, Glass Lewis will review, on a case-by-case basis, proposals that request that companies disclose their median gender pay ratios (as opposed to proposals asking that such information be adjusted based on factors such as job title, tenure and geography). Glass Lewis will generally recommend voting against these proposals where companies have provided sufficient information concerning their diversity initiatives and how they are ensuring gender pay parity.

Compensation-Related Policies

Contractual Payments and Arrangements. Glass Lewis clarified its policy on contractual payments and arrangements by highlighting executive employment terms that may drive a negative say-on-pay recommendation, including excessively broad change-in-control triggers, inappropriate severance entitlements, inadequately explained or excessive sign-on arrangements, guaranteed bonuses (especially multi-year), and the failure to address any concerning practices in amended employment agreements.

Change in Control. Glass Lewis clarified that it considers double-trigger change-in-control arrangements, which require both a change-in-control and an employment termination or constructive termination, to be best practice, and that any arrangement that is not explicitly double-trigger may be considered a single-trigger or modified single-trigger arrangement. In addition, Glass Lewis believes that excessively broad definitions of change-in-control are potentially problematic.

Short-Term Incentives. Glass Lewis clarified its policy relating to short-term incentives by indicating that, where a company has applied upward discretion (including where it lowers goals mid-year or increases calculated payouts), Glass Lewis expects a robust discussion of why the compensation committee felt it was necessary to exercise such discretion.

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If you have any questions about this Alert, please contact your usual legal advisor at Ropes & Gray.