

SIDLEY UPDATE

ISS and Glass Lewis Proxy Voting Policy Updates for the 2023 Proxy Season

December 23, 2022

Proxy advisory firms Institutional Shareholder Services (ISS) and Glass Lewis & Co. (Glass Lewis) have updated their proxy voting policies for shareholder meetings held on or after February 1, 2023 (ISS) or January 1, 2023 (Glass Lewis).¹ This Sidley Update summarizes the most noteworthy changes ISS and Glass Lewis made to their policies that apply to U.S. companies and provides some practical considerations. Appendix A summarizes the various circumstances in which ISS and Glass Lewis may recommend votes against directors in an uncontested election.

ISS Policy Updates for 2023

The key changes to ISS' proxy voting policies for 2023 relate to the following:

- **Board Gender Diversity.** Beginning in 2023, ISS' existing board gender diversity policy, previously announced in 2021, will apply to all companies (not just Russell 3000 and S&P 1500 companies). For 2023, ISS will generally recommend votes against nominating committee chairs (or other directors on a case-by-case basis) at all companies where there are no women on the board. ISS will continue to make an exception if there was at least one woman on the board at the previous annual meeting and the board commits to return to a gender-diverse status within a year.
- **Officer Exculpation Charter Amendment Proposals.** The Delaware General Corporation Law (DGCL) was amended in August 2022 to permit corporations to limit or eliminate the personal liability of senior officers for claims of breach of the fiduciary duty of care (but not the duty of loyalty) by including an exculpation provision in the corporation's charter. Previously the DGCL allowed corporations to limit or eliminate such liability only for directors. For 2023, ISS will evaluate on a case-by-case basis proposals to amend the charter to provide for officer exculpation, taking into account the stated rationale for the proposed change and other specified factors. ISS added that it will consider the extent to which the proposal would eliminate directors' and officers' liability for monetary damages for violating the duty of loyalty (which is permitted in some states such as Nevada) but noted that it will generally not support proposals to adopt an officer exculpation charter provision that would apply to duty of loyalty breaches even if allowed under state law.
- **Board Accountability – Climate-Related Issues.** For 2023, ISS will expand the scope of its climate accountability policy to apply globally. Under the updated policy, ISS will generally recommend votes against the incumbent chair of the responsible committee (or other directors on a case-by-case basis) at companies that are significant greenhouse gas (GHG) emitters through their operations or value chain (i.e., companies in the [Climate Action 100+ Focus Group](#)) if ISS determines that the company has not taken minimum steps needed to assess and mitigate the company's climate-related risks. For purposes of the policy, minimum steps include both (1) detailed disclosure of climate-related risks, such as according to the framework established by the Task Force on Climate-related Financial Disclosures

¹ ISS, United States Proxy Voting Guidelines: Benchmark Policy Recommendations (published Dec. 13, 2022), available [here](#); Glass Lewis, 2023 Policy Guidelines: United States (published Nov. 17, 2022), available [here](#); and Glass Lewis, 2023 Policy Guidelines: ESG Initiatives (published Nov. 17, 2022), available [here](#).

(TCFD), and (2) appropriate GHG emissions reduction targets, meaning medium-term GHG reduction targets or Net Zero-by-2050 GHG reduction targets for a company's operations (Scope 1) and electricity use (Scope 2). ISS noted that the targets should cover the vast majority (95%) of the company's direct emissions.

- **Board Accountability – Unequal Voting Rights.** In 2023, ISS will generally recommend votes against individual directors, committee members or the entire board (except new nominees, who should be considered case-by-case) if a company uses a common stock structure with unequal voting rights, with limited exceptions for (1) newly-public companies with a sunset provision of not more than seven years from the date of going public, (2) limited partnerships and the operating partnership unit structure of REITs, (3) situations where the super-voting shares represent less than 5% of total voting power and are therefore considered to be *de minimis* or (4) cases where the minority shareholders have a binding vote on whether to maintain the structure. The revised policy reflects the expiration of the one-year grace period for companies that had been grandfathered under the current policy and now defines the *de minimis* exception to mean no more than 5% of the total voting power.
- **Board Accountability – Problematic Governance Structures.** Although ISS has recognized a reasonable sunset provision as a potential mitigating factor when making vote recommendations with respect to problematic governance structures, its policy had not explained what characteristics would render a sunset provision reasonable. To provide clarity, ISS updated its policy for 2023 to state that a problematic governance structure must sunset within seven years of the date of going public to be considered a mitigating factor.² Additionally, ISS clarified that the policy applies to companies that held their first annual shareholder meeting after February 1, 2015 (replacing the previous reference to “newly public companies”).
- **Board Accountability — Poison Pills.** For 2023, ISS revised its poison pill policy to clarify that it will consider the trigger threshold as an additional factor when evaluating the appropriateness of the board's actions in adopting a short-term pill that is not put to a vote. ISS [indicated](#) that it considers trigger thresholds of 5-10% very low.
- **Board Accountability – Unilateral Bylaw/Charter Amendments.** ISS generally recommends votes against directors (except new nominees, who should be considered case-by-case) if the board amends the company's bylaws or charter without shareholder approval in a way that materially diminishes shareholders' rights or could adversely impact shareholders. For 2023, ISS revised the policy to add two situations that may lead to negative vote recommendations: if the board adopted a fee-shifting provision³ or any other provision deemed egregious by ISS.
- **Shareholder Proposals to Reduce Quorum Requirements.** ISS relaxed its policy on amending quorum requirements after observing a recent increase in the number of small companies with large retail ownership that had to repeatedly adjourn their shareholder meetings due to the lack of a quorum. For 2023, ISS revised its policy to evaluate on a case-by-case basis proposals to reduce quorum requirements for shareholder meetings below a majority of the shares outstanding, considering specified factors. ISS prefers a quorum threshold as close as possible to a majority of shares outstanding. ISS will make vote recommendations on a case-by-case basis with respect to directors who unilaterally lower the company's quorum requirements below a majority of shares, taking into account specified factors and the immediate circumstances of the meeting/adjournments in progress.
- **Shareholder Proposals Requesting Racial Equity and/or Civil Rights Audits.** For 2023, ISS added as a new factor it will consider when evaluating on a case-by-case basis shareholder proposals requesting racial equity and civil rights audits whether a company adequately discloses workforce diversity and inclusion metrics and goals, which ISS believes will allow for quantitative assessments of progress.

² This aligns with ISS' proxy voting policy regarding problematic capital structures, which views a seven-year time-based sunset to a dual-class capital structure as reasonable.

³ A fee-shifting provision could require a shareholder who sues a corporation and loses to pay all litigation expenses of the corporation and its directors and officers.

- **Shareholder Proposals on Political Expenditures and Lobbying Congruency.** Under a new policy for 2023, ISS will evaluate on a case-by-case basis shareholder proposals requesting greater disclosure from companies about the alignment between their political contributions and lobbying efforts and their publicly stated values and policies. ISS will consider (1) the company's policies, management, board oversight, governance processes and level of disclosure related to political expenditures and lobbying activities, (2) the company's disclosure regarding the reasons for its support of candidates, trade associations and other political activities, (3) any incongruencies between a company's political expenditures and its publicly stated values and priorities and (4) recent significant controversies related to the company's lobbying or political contributions or activities. Additionally, ISS will evaluate on case-by-case basis proposals requesting comparison of a company's political spending to objectives that can mitigate material risks for the company (e.g., limiting global warming).
- **Share Issuance Mandates at U.S. Domestic Issuers Incorporated Outside the U.S.** For 2023, ISS implemented a new policy regarding share issuance mandates for U.S. domestic issuers incorporated outside the U.S. and listed *solely* on a U.S. exchange. For these issuers, ISS will generally recommend votes in favor of proposals to authorize the issuance of common shares up to 20% of currently issued common share capital where the issuance is not connected to a specific transaction or financing proposal. ISS will evaluate case-by-case proposals to authorize share issuances tied to a specific transaction or financing proposal. For pre-revenue or other early-stage companies that rely heavily on periodic equity financing, ISS will generally recommend votes in favor of proposals to authorize a common stock issuance of up to 50% of currently issued shares, with the company bearing the burden to prove there is a genuine need for the increased limit. ISS advises companies to seek renewal of these mandates annually.
- **Problematic Pay Practices.** ISS maintains a list of examples of problematic pay practices that carry significant weight in its consideration of a company's overall pay program and may result in negative vote recommendations. For 2023, ISS added as a new example severance payments made to an executive when the executive's termination is not clearly disclosed as involuntary (e.g., a termination without cause or resignation for good reason). ISS also clarified that the list is not exhaustive and referred to its [U.S. Compensation Policies: Frequently Asked Questions](#) for more detail.
- **Equity-Based and Other Incentive Plans — Value-Adjusted Burn Rate.** In its policy updates for 2022, ISS announced that it would be transitioning to a new "Value-Adjusted Burn Rate" methodology for stock plan evaluations. The change will be in effect for 2023 now that the one-year transition period has ended.
- **Shareholder Proposals on Environmental and Social Metrics in Executive Compensation.** For 2023, ISS will continue to evaluate on a case-by-case basis shareholder proposals seeking increased disclosure on a company's approach toward incorporating environmental and social (E&S) criteria into its executive compensation strategy, considering specified factors. ISS revised the policy to reflect its view that a company's board or compensation committee is generally in the best position to determine performance metrics while also acknowledging that shareholders would benefit from improved disclosure about the rationale and considerations behind pay metrics.

Glass Lewis Policy Updates for 2023

The key updates to Glass Lewis' proxy voting policies for 2023 relate to the following:

- **Board Gender Diversity.** As announced in 2022, Glass Lewis will transition from a fixed numerical approach to a percentage-based approach for board gender diversity in 2023. At Russell 3000 companies, Glass Lewis will generally recommend votes against the nominating committee chair of a board that is not at least 30% gender diverse. Glass Lewis will review a company's disclosure of its diversity considerations and may choose not to issue negative vote recommendations if a board has provided a sufficient rationale or plan to address the lack of board diversity, including a timeline to appoint gender diverse directors (generally by the next annual meeting).

- **Underrepresented Community Board Diversity.** Beginning in 2023, at Russell 1000 companies, Glass Lewis will generally recommend votes against the nominating committee chair of a board with no director from an “underrepresented community.”⁴ Glass Lewis will review a company’s disclosure of its diversity considerations and may choose not to issue negative vote recommendations if a board has provided a sufficient rationale or plan to address the lack of board diversity, including a timeline to appoint additional directors from an underrepresented community (generally by the next annual meeting).
- **State Laws on Board Diversity.** Two California state laws mandating gender and underrepresented community diversity on the boards of California-headquartered corporations were struck down as unconstitutional in spring 2022. Those decisions have been appealed. Glass Lewis clarified that while it follows the appeal process, it will continue to monitor a company’s compliance with state board composition requirements but will not issue vote recommendations until further notice.
- **Disclosure of Director Diversity and Skills.** Beginning in 2023, Glass Lewis will expand from the S&P 500 to the Russell 1000 its policy to generally recommend votes against the nominating and/or governance committee chair at companies that have not provided any disclosure in their proxy statements in any of the following categories: (1) the board’s current percentage of racial/ethnic diversity, (2) whether the board’s definition of diversity explicitly includes gender and/or race/ethnicity, (3) whether the board has adopted a “Rooney Rule” policy requiring women and minorities to be included in the initial pool of candidates when selecting new director nominees and (4) board skills disclosure. In addition, beginning in 2023, Glass Lewis will generally recommend votes against the nominating and/or governance committee chair at Russell 1000 companies that have not provided any disclosure of individual or aggregate racial/ethnic minority demographic information.
- **Director Commitments.** Glass Lewis revised its policy on director commitments to establish different thresholds for a director who serves as an executive *officer* of a public company versus an executive *chair*. As revised for 2023, Glass Lewis will generally recommend votes against (1) a director who serves as an executive officer (other than executive chair) of any public company while serving on more than one external public company board, (2) a director who serves as an executive chair of any public company while serving on more than two external public company boards and (3) any other director who serves on more than five public company boards. Glass Lewis will continue to consider other relevant factors (e.g., size and location of the other companies, director tenure, meeting attendance) in determining whether a director’s service on an excessive number of boards may limit the ability of the director to devote sufficient time to board duties. Glass Lewis generally will not recommend votes against overcommitted directors at the companies where they serve as an executive. Finally, Glass Lewis clarified that it will generally refrain from recommending votes against a director who serves on an excessive number of boards within a consolidated group of companies *in related industries*.
- **Officer Exculpation Charter Amendment Proposals.** Glass Lewis will generally recommend votes against officer exculpation charter amendment proposals unless the board provides a compelling rationale for the adoption and the provisions are reasonable.
- **Board Accountability – Climate-Related Issues.** For companies with material exposure to climate risk stemming from their own operations (i.e., companies in the Climate Action 100+ Focus Group), Glass Lewis expects thorough climate-related disclosures in line with TCFD recommendations and disclosure of explicit and clearly defined oversight responsibilities for climate-related issues. If these disclosures are absent or significantly lacking, Glass Lewis may recommend votes against the chair of the committee (or board) charged with oversight of climate-related issues, or if no committee has been charged with oversight, the governance committee chair. Glass Lewis may extend its negative vote recommendation to additional members of the responsible committee if the committee chair is not standing for election due to a classified board, or based on other factors (e.g., the company’s size, industry and overall governance profile). If appropriate directors are not standing for election, Glass Lewis may instead

⁴ As defined by Glass Lewis, a director from an “underrepresented community” is an individual who self-identifies as (x) Black, African American, North African, Middle Eastern, Hispanic, Latino, Asian, Pacific Islander, Native American, Native Hawaiian or Alaskan Native or (y) gay, lesbian, bisexual or transgender. For purposes of the evaluation, Glass Lewis will rely solely on the self-identified demographic information disclosed in a company’s proxy statement.

recommend votes against other voting items (e.g., ratification of board acts).

- **Board Oversight of E&S Issues.** Beginning in 2023, Glass Lewis will generally recommend votes against the governance committee chair of Russell 1000 companies that fail to provide explicit disclosure in their proxy statements or governance documents (e.g., committee charters) about the board's role in overseeing E&S issues. In 2023, Glass Lewis will expand tracking of board-level oversight of E&S issues to all companies within the Russell 3000 index but will not yet issue vote recommendations beyond Russell 1000 companies.
- **Board Oversight of Cyber Risk.** Glass Lewis views cyber risk as material for all companies and encourages companies to provide clear disclosure concerning the role of the board in overseeing issues related to cybersecurity and how directors are staying well-informed on evolving cybersecurity issues. In 2023, Glass Lewis will generally not issue vote recommendations on the basis of a company's oversight or disclosure concerning cyber-related issues but may recommend votes against appropriate directors at a company where cyber-attacks have caused significant harm to shareholders and Glass Lewis finds that the disclosure or oversight is insufficient.
- **Disclosure of Shareholder Proponents.** Glass Lewis will generally recommend votes against the governance committee chair if a company does not disclose in its proxy statement the identity of the proponent (or lead proponent when multiple proponents have submitted a proposal) of any shareholder proposal that may be going to a vote. Glass Lewis also encourages companies to provide information about the proponent's level of share ownership and the company's engagement (or lack thereof) with a proponent.
- **Shareholder Proposals Requesting Racial Equity or Civil Rights Audits.** In a new policy for 2023, Glass Lewis has codified its approach to shareholder proposals requesting that companies undertake racial equity or civil rights audits. When analyzing these proposals, Glass Lewis will assess (1) the nature of the company's operations, (2) the level of disclosure provided by the company and its peers on its internal and external stakeholder impacts and the steps it is taking to mitigate any attendant risks and (3) any relevant controversies, fines or lawsuits. Thereafter, Glass Lewis will generally recommend votes in favor of a well-crafted proposal when doing so could help the target company identify and mitigate potentially significant risks.
- **Board Responsiveness.** Glass Lewis clarified its expectations for board responsiveness when a significant percentage of shareholders vote contrary to management, as evidenced by votes against a director nominee or management proposal or votes for a shareholder proposal. When 20% or more shareholders vote contrary to management, boards should engage with shareholders on the issue and demonstrate some initial level of responsiveness, and when a majority of shareholders vote contrary to management, boards should engage with shareholders and provide a more robust response to fully address shareholder concerns. This may include fully implementing the request of a majority-supported shareholder proposal and/or engaging with shareholders on the issue and providing sufficient disclosures to address shareholder concerns. Glass Lewis also expanded its evaluation of board responsiveness to include a review of a company's proxy statement disclosure describing the board's efforts to engage with shareholders and the actions taken to address shareholder concerns.
- **Compensation Clawback Provisions.** On October 26, 2022, the SEC adopted rules mandating that the national securities exchanges develop new listing standards requiring listed companies to maintain and disclose compensation clawback policies. The New York Stock Exchange and Nasdaq must update their listing standards by November 28, 2023 in response to the final rules, and companies will have 60 days after the effective date of the new listing standards to comply. Until the new listing standards take effect, Glass Lewis will continue to raise concerns for companies that maintain clawback policies that meet only the requirements set forth by Section 304 of the Sarbanes-Oxley Act. However, Glass Lewis noted that disclosure about proactive efforts to meet the standards of the final rules may help to mitigate concerns. Glass Lewis recommends that boards adopt detailed variable compensation clawback policies that, at a minimum, allow companies to recover compensation from former and current named executive officers in the event of overpayment due to erroneous data that triggered an accounting restatement. Glass Lewis noted that it will increase its focus on the specific terms of clawback policies – beyond merely

satisfying minimum legal requirements – as market practice continues to evolve.

- **Other Compensation-Related Policy Updates:**

- **Incentive Programs:** Glass Lewis revised its threshold for the minimum percentage of the long-term incentive grant that should be performance-based from 33% to 50% to align with market trends. Accordingly, beginning in 2023, Glass Lewis will raise concerns in its analysis with executive pay programs that provide that less than half of an executive's long-term incentive awards are subject to performance-based vesting conditions. Further, Glass Lewis updated its discussion of short- and long-term incentives to recognize the importance of the compensation committee's judicious and responsible exercise of discretion over incentive pay outcomes to account for significant, material events (e.g., major litigation settlement charges or health and safety failures) that would otherwise be excluded from performance results of selected metrics of incentive programs. Glass Lewis believes that companies should discuss how these events were considered in the committee's decisions to exercise discretion or refrain from applying discretion over incentive pay outcomes.
- **Compensation Committee Performance:** Glass Lewis clarified that beginning in 2023 it will consider recommending votes against the compensation committee chair when a company grants "mega-grants" (meaning outsized awards to one individual valued at more than \$100 million) that present concerns such as excessive quantum, lack of sufficient performance conditions and/or excessive dilution, among others.
- **Grants of Front-Loaded Awards:** Glass Lewis expanded its discussion relating to front-loaded awards, which it weighs with particular scrutiny, to explicitly reference "mega-grants." Glass Lewis also expanded on its concerns regarding the increased restraint placed on the board to respond to unforeseen factors when a company uses front-loaded awards. Finally, Glass Lewis clarified that in situations where a front-loaded award was intended to cover a certain portion of the regular long-term incentive grant for each year during the covered period, Glass Lewis' analysis of the value of the remaining portion of the regular long-term incentives granted during the period covered by the award will account for the annualized value of the front-loaded portion and Glass Lewis expects the company will not award a supplemental grant during the vesting period of the front-loaded portion.
- **One-Time Awards:** Glass Lewis has expanded its expectations regarding a company's disclosure of one-time awards and beginning in 2023 will expect a company to describe how it determined the quantum and structure of the award.
- **Pay for Performance:** Glass Lewis noted that it may review new pay-for-performance disclosures when evaluating executive pay programs on a qualitative basis but clarified that the new SEC rules will not change Glass Lewis' pay-for-performance methodology for the 2023 proxy season.
- **Company Responsiveness to Say-on-Pay:** Glass Lewis clarified its policies on company responsiveness to shareholder opposition of more than 20% to say-on-pay proposals. When assessing the level of opposition, Glass Lewis added that it may examine the level of opposition among disinterested shareholders as an independent group. Glass Lewis expects a board to demonstrate a commensurate level of engagement and responsiveness to the concerns behind the disapproval, with a particular focus on responding to shareholder feedback. Appropriate responses include engaging with large shareholders, especially dissenting shareholders, to identify their concerns, and, where reasonable, implementing changes and/or making commitments that directly address those concerns within the company's compensation program. In cases where particularly egregious pay decisions caused the say-on-pay proposal to fail, Glass Lewis will closely consider whether any changes were made directly relating to the pay decision that may address structural concerns that shareholders have.
- **Retirement Benefits and Severance:** In an update for 2023, Glass Lewis clarified that, while it generally supports proposals requesting that companies adopt a policy whereby shareholders must approve severance payments exceeding 2.99 times the amount of the executive's base salary plus bonus, it may recommend against them if the company has a policy to seek shareholder approval for any cash severance payments exceeding 2.99 times the sum of an executive's salary and bonus.

Practical Considerations

- Companies should review the composition of their boards and their corporate governance and compensation practices for potential vulnerabilities under the ISS and Glass Lewis policy updates (e.g., in relation to board gender and racial/ethnic diversity or director commitments) and decide what action, if any, to take in light of this assessment.
- Companies should consider supplementing their proxy statement disclosures in light of the policy updates for 2023, particularly with respect to director diversity and board oversight of climate-related, E&S and cybersecurity issues. They should also be sure to identify the proponents of any shareholder proposals listed in the proxy statement.
- Finally, companies incorporated in Delaware should consider amending their charters to add an officer exculpation provision, which would require seeking shareholder approval at their next annual meeting.

If you have any questions regarding this Sidley Update, please contact the Sidley lawyer with whom you usually work, or

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