Glass Lewis Publishes Updates to 2021 U.S. Voting Policy Guidelines

Glass Lewis & Co., Inc. has published updates to its voting policy guidelines for U.S. companies for the 2021 proxy season. In addition to various changes and clarifications to certain of its compensation-related policies, Glass Lewis also made updates to its policies related to the composition of the Board of Directors. These latter changes are in keeping with a spate of recent developments in board diversity at the state level (most recently in California and Washington state) and changes proposed by NASDAQ that would require all listed companies to disclose board diversity statistics.

We expect that the updated Glass Lewis guidelines will be effective for annual meetings of shareholders held on or after January 1, 2021.

Compensation-Related Policy Updates

Short-Term Incentive Plans

In anticipation of the fact that many 2020 short-term incentive plans will have been changed or modified as a result of the COVID-19 pandemic, Glass Lewis has codified several additional factors that it will consider in evaluating such plans. Specifically, Glass Lewis expects clearly disclosed justifications to accompany any significant changes to a company's plan structure, as well as any instances in which performance goals have been lowered from the previous year. In addition, it has expanded its description of the application of upward discretion to include instances of retroactively pro-rated performance periods. Any such changes are likely to be reviewed in the context of other actions taken by companies (such as employee layoffs or furloughs and pay reductions) as part of their efforts to control costs in a volatile environment.

Long-Term Incentive Plans

Generally, Glass Lewis prefers that a significant portion of executives' long-term incentive awards be performance-based. While it consistently raises concerns about plans that do not meet this condition, it may refrain from a negative vote recommendation in the absence of other significant issues with the plan's design or operation. In addition, as part of its update Glass Lewis has codified additional factors it will consider in assessing the structure of a long-term incentive plan. Specifically, it has defined inappropriate performance-based award allocations as a criterion which may, in the presence of other major concerns, contribute to an adverse vote recommendation. In addition, any decision to significantly roll back or eliminate performance-based awards will be reviewed as a regression of best practices, that outside of exceptional circumstances, may lead to an adverse vote recommendation. Finally, Glass Lewis has indicated that clearly disclosed explanations are expected to accompany long-term incentive equity granting practices, as well as any significant structural plan changes or any use of upward discretion.

Other Compensation Policy Clarifications

In addition to the foregoing, Glass Lewis has clarified certain aspects of its current executive compensation policy guidelines as follows:

- *Excise tax gross-ups and votes on golden parachute payments* – Glass Lewis has added language to its policy on excise tax gross-ups to make clear that the addition of new excise tax gross-up provisions in connection with specific change-in-control transactions will be problematic. In this situation, in addition to issuing an adverse vote recommendation for the golden parachute proposal in which the gross-up entitlements first appear, it may also issue an adverse vote recommendation with respect to the compensation committee members who approved the provisions and the Say-on-Pay proposals of any of the involved corporate parties.
- *Option exchanges and repricing* – Glass Lewis has added language to its policy on evaluating stock option exchanges and repricing proposals which emphasizes the exclusion of officers and members of the board of directors from the program, as well as a statement that the program be value-neutral or value-creative, in influencing any decision to make an exception to its general opposition to such proposals.
- *Peer group methodology* – Glass Lewis has clarified that, in determining the peer groups used in its pay-for-performance model (under which companies are assigned a letter grade), it uses a

previously-announced proprietary methodology (with the relevant data provided by its partner, CGLytics) in which it considers both country-based and sector-based peers, along with each company's network of self-disclosed peers. Each component is considered on a weighted basis and is subject to size-based ranking and screening.

Notable Governance Policy Updates

Board Gender Diversity

Beginning in 2021, Glass Lewis will note as a concern boards of directors that contain fewer than two female members. Its voting recommendations in 2021 will continue to be based on its current requirement of at least one female board member. However, beginning with annual meetings of shareholders held after January 1, 2022, Glass Lewis will generally issue an adverse vote recommendation against the nominating committee chair of a board of directors with less than two female directors. In the case of a board of directors with six or fewer total members, the existing voting policy requiring a minimum of one female director will remain in place.

Consistent with its current policy, Glass Lewis may extend this recommendation to additional members of the nominating committee in cases where the committee chair is not standing for election due to a classified board, or based on other factors, including the company's size and industry, applicable laws in its state of headquarters, and its overall governance profile. When making these voting recommendations, Glass Lewis will carefully review a company's disclosure of its diversity considerations and may refrain from recommending that shareholders vote against directors of companies outside the Russell 3000 index, or when boards have provided a sufficient rationale or plan to address their lack of diversity.

State Laws on Diversity

In addition to its standard policy on board diversity, Glass Lewis will also base its voting recommendation in accordance with board composition requirements set forth in applicable state laws when and as they come into effect. For example, in 2018, California enacted a board gender diversity requirement which requires publicly held companies with their principal executive offices in the state to have at least one female director and, by December 31, 2021, multiple female directors if they have five or more directors. And, earlier this year, California passed a law that requires publicly held companies headquartered in the state to meet a board of directors' "underrepresented community" diversity quota of at least one director by December 31, 2021 and requires more than one member of underrepresented communities on the Board by December 31, 2022 (up to a maximum of three for boards with nine or more members). Consequently, in the case of annual meetings of shareholders taking place after December 31, 2021, Glass Lewis will generally issue an adverse vote recommendation for the chair of the nominating committee of a California-headquartered company that does not meet these minimum standards.

Director Diversity and Skills Disclosure

Beginning with the 2021 proxy season, Glass Lewis reports for companies in the S&P 500 index will include an assessment of companies' proxy statement disclosure relating to board diversity, skills, and the director nomination process. Specifically, Glass Lewis will disclose how a company's proxy statement presents:

- the board's current percentage of racial/ethnic diversity;
- whether the board's definition of diversity explicitly includes gender and/or race/ethnicity;
- whether the board has adopted a policy requiring women and minorities to be included in the initial pool of candidates when selecting new director nominees; and
- board skills disclosure.

Glass Lewis will not be making voting recommendations solely on the basis of this assessment in 2021. Nonetheless, this rating will help inform its assessment of a company's overall governance and may be a contributing factor in its recommendations when additional board-related concerns have been identified.

Board Refreshment

Beginning in 2021, Glass Lewis will raise as a potential concern instances where the average tenure of non-executive directors is 10 years or more and no new independent directors have joined the board in the past five years. While it will not be making voting recommendations solely on this basis in 2021, Glass Lewis indicates that insufficient board refreshment may be a contributing factor in its recommendations when additional board-related concerns have been identified.

Observations

Glass Lewis' updates to its policies on short-term and long-term incentive plans reflect the practical reality that many companies made changes to their plans in response to the economic impact of the COVID-19 pandemic. Consequently, it will be closely scrutinizing these changes and expects that any significant changes to the plan structure will be accompanied by rationalizing disclosure. As it made clear in its policy statement earlier this year addressing how it would apply its voting guidelines in the wake of the pandemic, both the quality of the disclosure, as well as the justifications for specific decisions, are going to be evaluated when assessing the factors that led to the changes and determining whether the decisions were reasonable in terms of consistency and proportionality when compared to the pandemic's effect on shareholder interests and employees.

The policy updates also reflect the increased importance Glass Lewis is placing on environmental, social, and governance ("ESG") issues at the board level, particularly as it relates to enhanced disclosure in the proxy statement. In addition to bolstering its board gender diversity policy, beginning in 2021 its reports for S&P 500 companies will include an assessment of their disclosure relating to board diversity, skills and the director nomination process. Also beginning in 2021, Glass Lewis will note as a concern when boards of S&P 500 companies do not provide clear disclosure concerning the board-level oversight afforded to environmental and/or social issues. Beginning with shareholder meetings held after January 1, 2022, Glass Lewis will generally issue an adverse vote recommendation for the governance committee chair of an S&P 500 company that fails to provide explicit disclosure concerning the board's role in overseeing these matters.

For more information on these updates and to view the full slate of 2021 U.S. policy guidelines, click here.

About the Authors

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Need Assistance?

Compensia has extensive experience in assisting companies in addressing Glass Lewis' U.S. voting policy guidelines. If you would like assistance in analyzing the potential impact of the Glass Lewis policies on your executive compensation program, or if you have any questions on the subjects addressed in this Thoughtful Pay Alert, please feel free to contact Mark A. Borges, Jason Borrevik, or Alex Miller. ■

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