November 2019

CLIENT ALERT

ISS and Glass Lewis Publish 2020 Policy Updates

ISS and Glass Lewis recently published updates to their respective proxy voting policy guidelines for the 2020 proxy season. Additionally, ISS announced a major change to its pay-for-performance model; replacing GAAP financial metrics with Economic Value Added (EVA)-based performance metrics. The updated guidelines will be effective for all companies with annual meetings on or after February 1, 2020.

2020 ISS Compensation-Related Policy Updates

There are two main compensation-related updates that have been announced by ISS for its 2020 U.S. Proxy Voting Guidelines:

1. Economic Value Added (EVA)-based performance metrics replacing GAAP financial metrics in the Financial Performance Assessment (FPA) secondary screen of the pay-for-performance quantitative screen for U.S. and Canadian markets.
2. ISS added a new negative overriding factor to the U.S. Equity Plan Scorecard (EPSC) analysis. Equity plans containing an evergreen feature will now be viewed negatively and will generally lead to ISS recommending an against vote on the plan.

Pay-for-Performance Model – Effective February 1, 2020, ISS will compare compensation to four EVA metrics under the updated FPA pay-for-performance screen:

1. EVA Margin = *EVA/Sales*
2. EVA Spread = *EVA/Capital (average capital outstanding over the trailing four quarters)*
3. EVA Momentum vs. Sales = *the Change in EVA/Prior Year Sales*
4. EVA Momentum vs. Capital = *the Change in EVA/Prior Year Capital*

Additionally, the thresholds that trigger concern on the Relative Degree of Alignment and Pay-TSR Alignment tests will be updated to reflect the new EVA metrics. ISS plans to release an additional publication that will deliver greater detail regarding the introduction of EVA metrics in December 2019.

Equity-based and Other Incentive Plans – ISS has added a new negative overriding factor to its EPSC analysis so that equity plans which have an evergreen feature will now automatically be viewed negatively. This is in response to the Tax Cuts and Jobs Act of 2017, which repealed the performance-based exemption on executive compensation and eliminated the need for companies to obtain regular shareholder reapproval of equity plans.

Links: U.S. Proxy Voting Guidelines Updates for 2020

U.S. Compensation Policies Preliminary FAQs for 2020

U.S. Benchmark Policy Updates and Process

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2020 GLASS LEWIS COMPENSATION-RELATED POLICY UPDATES

Compensation-related policy modifications announced by Glass Lewis were minimal and mainly focused on clarifying existing policies.

Company Responsiveness – In response to low say-on-pay ("SOP") vote support, Glass Lewis now expects a robust disclosure of engagement activities and specific changes made in response to shareholder feedback. The company may receive a vote against the upcoming SOP proposal if the level of responsiveness is not viewed as appropriate to the severity and persistence of shareholder opposition.

Contractual Payments and Arrangements – Generally, agreements that are excessively restrictive in favor of the executive, including excessive severance payments, new or renewed single-trigger change-in-control arrangements, excise tax gross-ups or multi-year guaranteed awards will be seen as unfavorable.

Post-Fiscal Year End Compensation Decisions – Significant changes or modifications to compensation plans, including post-fiscal year end changes and one-time awards will be reviewed on a case-by-case basis. Such a review will take place particularly in the instances where the changes touch upon issues that are material to Glass Lewis recommendations.

Pay-for-Performance – Compensation and performance are measured against a peer group of appropriate companies that may overlap with a company's self-chosen group. Overall incentive structure, disclosure of significant changes to the compensation program or reasonable long-term payout levels may mitigate some concerns, but companies that demonstrate a weaker link between pay and performance are more likely to receive a negative SOP vote recommendation.

Mid-Year Adjustments to Short-Term Incentive Plans – When a company has applied upward discretion, which includes lowering goals mid-year or increasing calculated payouts, it is expected that a robust discussion of why the decision was necessary be provided.

Change-in-Control Definitions – Excessively broad definitions of change-in-control are potentially problematic as they may lead to situations where executives receive additional compensation when no meaningful change in status or duties has occurred.

Link: Glass Lewis 2020 Proxy Paper Guidelines

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ABOUT STEVEN HALL & PARTNERS

Steven Hall & Partners is an independent executive compensation consulting firm, specializing exclusively in the areas of executive compensation, board remuneration, non-profit compensation and related governance issues. By focusing solely on this critical and complex segment of the human resources arena, we are able to provide our clients with the highest quality expertise and best counsel available on a practical basis. For more information, please visit www.shallpartners.com and follow us on Twitter @SHallPartners.

CONTACTING STEVEN HALL & PARTNERS

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Contact

Steven Hall Jr.

212-488-5400

sehall@shallpartners.com

Devin Reilly

212-488-5400

dreilly@shallpartners.com

William Fiske

212-488-5400

wfiske@shallpartners.com