GLASS LEWIS 2021 Policy Updates

UK & Europe

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INTRODUCTION

On 24 November 2020, Glass Lewis released its guidelines updates for its main voting policies for 2021[1]. The updates will be effective from the 2021 AGM season and apply to all shareholder meetings thereafter. Our memo summarizes the policy changes that will be applied across UK & Ireland and Continental Europe.

Across the board, the main changes relate to environmental and social risk oversight, environmental and social initiatives, board diversity and remuneration. Below we have sought to provide a brief but thorough review of the main changes.

UK & Continental Europe

ENVIRONMENTAL AND SOCIAL RISK OVERSIGHT

Under the updated guidelines and starting in 2021, Glass Lewis "will note as a concern when boards of companies listed on a major European blue-chip index 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, we will generally recommend voting against the governance chair of these boards which fail to provide explicit disclosure concerning the board's role in overseeing these issues." For the UK, this provision will apply in regard to companies included in the FTSE100 index.

While they recognize that oversight duties fall on the whole board, Glass Lewis also states that "companies should determine the best structure for this oversight for themselves. In our view, this oversight can be effectively conducted by specific directors, the entire board, a separate committee, or combined with the responsibilities of a key committee."

ENVIRONMENTAL AND SOCIAL INITIATIVES

Under its updated guidelines, Glass Lewis states that they "generally support shareholder proposals that seek to improve governance structures or promote relevant disclosure that serves the long-term interests of shareholders" and that they will assess these "shareholder proposals on environmental and social issues in the context of financial materiality."

HUMAN CAPITAL MANAGEMENT

Under the updated guidelines, Glass Lewis states that "companies should provide shareholders with adequate information to be able to assess the oversight of this critical aspect of their operations, and the mitigation of any attendant risks." A recommendation "against the chair of the governance committee (or equivalent), the chair of the board, and/or board ratification proposals as appropriate" will result in egregious cases where "boards have failed to respond to legitimate concerns regarding a company's policies, practices and disclosure".

For the UK, Glass Lewis also notes that "the UK Code recommends that the boards of premium-listed companies establish a mechanism for engaging the workforce in board discussions and decision-making. Specifically, boards are recommended to i) allow for the appointment of an employee representative to the board; ii) establish a formal workforce advisory panel; iii) designate a non-executive director to represent the views of the workforce; or iv) establish an alternative arrangement. In addition to disclosing the chosen method, we believe that FTSE 350 companies should also provide meaningful disclosure on an annual basis regarding the implementation of their workforce."

1) https://www.glasslewis.com/2021-glass-lewis-policy-guidelines-updates-now-available-for-north-america-europe-uk-and-japan/

VIRTUAL SHAREHOLDER MEETINGS

Under its updated guidelines, Glass Lewis states that it "unequivocally supports companies facilitating the virtual participation of shareholders in general meetings" while recognising that virtual-only shareholder meetings can "curb the ability of a company's shareholders to participate in the meeting and meaningfully communicate with company management and directors."

As such, the updated guidelines now include provisions as to the appropriateness of the meeting format and convocation which should ensure that "shareholders will have an opportunity to ask questions related to the subjects normally discussed at the annual meeting" and that "where there are restrictions on the ability of shareholders to question the board during the meeting the manner in which appropriate questions received during the meeting will be addressed by the board; this should include a commitment that questions which meet the board's guidelines are answered in a format that is accessible by all shareholders, such as on the company's AGM or investor relations website."

Where these principles are not respected, Glass Lewis will recommend that "shareholders vote against members of the governance committee (or equivalent; if up for re-election); the chair of the board (if up for re-election); and/or other agenda items concerning board composition and performance as applicable (e.g. ratification of board acts)" depending on the relevant governance structure.

In case amendments to the articles of association of a company are necessary for it to hold the meeting virtually, Glass Lewis expects that the amended provisions require at least that:

- "The procedure and requirements to participate in a virtual-only meeting will be disclosed at the time of convocation; and
- There will be a formal process in place for shareholders to submit questions to the board, which will be answered in a format that is accessible to all shareholders."

If the amendment provides that virtual-only meetings "would only be used in exceptional circumstances" Glass Lewis will normally supports the proposal.

As for hybrid meetings, "Glass Lewis will generally support proposed amendments that would allow for companies to hold hybrid meetings."

Lastly, Glass Lewis will likely oppose "the virtual attendance of directors and top-tier executives at traditional in-person or hybrid general meetings" as this "may serve to reduce accountability to shareholders and risks perpetuating the perception that companies are utilising emerging technologies to avoid uncomfortable conversations." As such, Glass Lewis will only allow virtual attendance of the senior leadership in virtual-only meetings or other meetings held in extraordinary circumstances.

UK & Ireland

BOARD AND WORKFORCE DIVERSITY

Gender diversity

Under their updated policy guidelines, Glass Lewis now requires that "boards of FTSE 350 companies to have met the target set by the Hampton-Alexander Review of 33% of board positions to be held by women by 2020. Further, we generally expect the boards of all UK- listed companies on the LSE's main market to contain at least one female director. Where a proposed board election does not align with these targets, we will generally recommend that shareholders vote against the re-election of the chair of the nomination committee (or equivalent)."

Exceptions will be made only for companies with board comprised of four or fewer board members or for companies that disclose a credible plan to address the gender imbalance or "otherwise demonstrate their commitment through an exceptionally diverse board."

Ethnicity and national origin

Additionally, under the revised guidelines, Glass Lewis states that "the composition of a board should be representative of a company's workforce, the jurisdictions in which it principally conducts its business activities, and its other key stakeholders." Therefore Glass Lewis believes that "boards should consider including diversity of ethnicity and national origin as attributes in their composition profiles, whether defined targets for diversity of ethnicity and national origin should be set, and the manner and extent to which the ethnic and national backgrounds of directors and board nominees is publicly disclosed."

For FTSE 350 companies, Glass Lewis states that they expect constituent companies "to provide meaningful disclosure regarding their performance against the Parker Review target31 that FTSE 100 companies and FTSE 250 companies should include "at least one director of colour" by 2021 or 2024, respectively. In 2021, Glass Lewis will begin highlighting where FTSE 350 companies have failed to provide meaningful disclosure in this regard and, in future years, will consider recommending that shareholders vote against the re-election of the chair of the nomination committee where disclosure and/or performance does not improve."

A negative recommendation on the re-election of the chair of the nominating committee (or equivalent) may be triggered in "egregious cases where a board has failed to address legitimate shareholder concerns regarding the diversity of ethnicity and national origin at board level".

Skills and experience

For FTSE 350 companies, Glass Lewis expects companies to provide a "a robust, meaningful assessment of the board's profile in terms of skills and experience in order to align with developing best practice standards." Egregious cases of lack of disclosure may trigger a recommendation against the chair of the remuneration committee or, when it is unclear how a new nominee will address the skills gap, in a recommendation against the same nominee.

ALIGNMENT OF REMUNERATION WITH STAKEHOLDER EXPERIENCE

With regard to remuneration, the updated guidelines, specify that Glass Lewis believes "remuneration outcomes should remain appropriate to a company's specific situation and the experiences of its shareholders and employees, even where formulaic targets have been met." Specifically, downward discretion is expected in the following cases:

- "A company has suffered an exceptional negative event that has had a material negative impact on shareholder value; or
- A company's decisions regarding working conditions have had a material negative impact on employees."

"In cases of substantial misalignment between executive pay outcomes and the experience of shareholders or employees in the past fiscal year, we may recommend that shareholders vote against a company's remuneration report solely on this basis."

Furthermore, the updated guidelines also specify that "forward-looking decisions regarding executive remuneration should also take into account the experience of shareholders and employees. We may recommend that shareholders vote against the remuneration policy where there is evidence that executive fixed pay and/or total opportunity increases are substantially outpacing employee salary increases."

SMALLER PREMIUM LISTED COMPANIES

For smaller premium listed companies, Glass Lewis will cease to apply softer requirements than the ones required for FTSE 350 companies. In particular, "in line with the recommendations of the UK Code, we expect

the boards of all premium-listed UK companies (i) to be at least 50% independent; and (ii) to hold annual, rather than staggered, director elections."

INVESTMENT COMPANY BOARDS

In its updated guidelines, Glass Lewis outlines that given the narrower remit of boards of investment companies, Glass Lewis will apply exceptions to its "policies regarding the external commitments of a director where a director serves on the boards of multiple investment companies" while specifying that "it is incumbent on the board to provide context on the nature of the roles held by a potentially overcommitted director."

Continental Europe

BOARD AND WORKFORCE DIVERSITY

Gender diversity

Under their updated policy guidelines, Glass Lewis now requires that "in countries that have well-established gender quotas in law or best practice [the board] should be composed of at least 30% of directors of each gender. In any case, we expect the boards of all companies on mid-cap or large-cap European indices to meet this standard by 2022."

Further, Glass Lewis now also states that companies listed on any main European market "should not be composed solely of directors of the same gender." Failure to comply with this standard, will trigger Glass Lewis to "recommend that shareholders vote against the chair of the nominating committee (or equivalent) or a new nominee to the board, as appropriate" while exceptions will be made only for companies with board comprised of four or fewer board members or for companies that "present a credible, near-term plan to address the lack of gender diversity on the board."

Ethnicity and national origin

Additionally, under the revised guidelines, Glass Lewis states that "the composition of a board should be representative of a company's workforce, the jurisdictions in which it principally conducts its business activities, and its other key stakeholders." Therefore Glass Lewis believes that "boards should consider including diversity of ethnicity and national origin as attributes in their composition profiles, whether defined targets for diversity of ethnicity and national origin should be set, and the manner and extent to which the ethnic and national backgrounds of directors and board nominees is publicly disclosed."

A negative recommendation on the re-election of the chair of the nominating committee (or equivalent) may be triggered in "egregious cases where a board has failed to address legitimate shareholder concerns regarding the diversity of ethnicity and national origin at board level".

Skills and experience

On skills and experience, Glass Lewis expects companies to provide a "a robust, meaningful assessment of the board's profile in terms of skills and experience in order to align with developing best practice standards." Egregious cases of lack of disclosure may trigger a recommendation against the chair of the nomination committee or, when it is unclear how a new nominee will address the skills gap, in a recommendation against the same nominee.

DIRECTOR AGE/TERM LIMITS

Under its new guidelines, Glass Lewis "will no longer generally recommend withholding support from proposals that seek to introduce or amend director age or term limits in line with prevailing market practice."

However, they also state that "where age/term limits exist, these should be applied equally to all directors." Therefore, if "a board waives its age/term limits, Glass Lewis will consider recommending shareholders vote against the chair of the nominating committee or equivalent, unless compelling rationale is provided for why the board is proposing to waive this rule through an election/re-election."

REMUNERATION COMMITTEE DISCRETION AND STAKEHOLDER ALIGNMENT

Remuneration policy

Under its updated guidelines, Glass Lewis has added few newer potential issues which could trigger a negative review and recommendation of a company's remuneration policy. In particular, the following issues are added to the list as troubling issues capable of triggering a negative recommendation:

- Discretion retained by the board is not limited to clearly-defined circumstances
- No portion of variable remuneration is linked to multi-year, forward-looking vesting conditions
- The policy does not include structural safeguards and risk mitigating features, such as clawback/ malus provisions, deferral, post-vesting holding periods, and post-employment shareholding requirements

On discretion in particular Glass Lewis expects that remuneration committees "should retain a reasonable level of discretion to ensure that pay outcomes are justified and linked to performance, and that the implementation of the remuneration policy remains appropriate, including with reference to performance metrics and specific targets. The scope of potential discretionary powers, and any exercise of such discretion made during the year, should be clearly disclosed and justified." Discretion is expected to be used specifically in the following cases:

- "A company has suffered an exceptional negative event that has had a material negative impact on shareholder value;

  For example, we generally expect a remuneration committee to consider reducing an annual bonus payout and/or the size of an LTI grant following a significant decline in share price. Further, we expect downward adjustments to the outcomes of awards linked to share price performance where windfall gains have been received; or

- A company's decisions regarding working conditions have had a material negative impact on employees;

  For example, we generally expect substantial workforce layoffs, furloughs, short-time working arrangements, salary freezes etc. to be reflected in executives' remuneration outcomes."

In this regard, Glass Lewis also states that "in cases of substantial misalignment between executive pay outcomes and the experience of shareholders or employees in the past fiscal year, we may recommend that shareholders vote against a company's remuneration report solely on this basis."

On a relative note, Glass Lewis may also raise concerns on a company's remuneration policy "where there is evidence that executive fixed pay and/ or total opportunity increases are substantially outpacing employee salary increases."

CONTINENTAL EUROPE

REMUNERATION REPORT

In regard to the remuneration report, Glass Lewis' guidelines now state that the annual remuneration vote should be used to "express concern with a company's remuneration policies and practices that are not explicitly limited to the year under review."

Adding more detail, the updated guidelines have harshened on the lowering of targets as any language regarding the possibility to do so with compelling justification have been expunged.

ANTI-TAKEOVER DEVICES

While Glass Lewis generally opposes the use of anti-takeover devices by companies, in their updated guidelines they state that "in extraordinary circumstances, we may recommend shareholders vote for proposals that are limited in timing and scope to accomplish a particular objective such as the closing of an important merger. We will also take into account any exceptional justification provided by the board, including contextual factors such as a severe drop in stock price due to a widespread industry or market downturn."

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