Aon Hewitt
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Glass Lewis Updates its US Compensation & Governance Policies for the 2016 Proxy Season

While Glass Lewis did not make major compensation policy changes, it did clarify its approach for evaluating one-off grants and announced a number of governance-related updates.

Glass Lewis & Co. ("Glass Lewis") published its 2016 proxy season policy updates for the US market on November 13, 2015. Unlike prior years, the updated policies were not announced on the Glass Lewis blog or on the corporate webpage. Instead, corporate and investor subscribers were alerted to the policy updates via an email announcement. Consistent with the prior year changes for the 2015 proxy season, Glass Lewis did not make any material executive compensation related policy changes, but instead, simply provided more context around the firm's evaluation of one-off grants of cash and equity to "Named Executive Officers" ("NEOs") and regarding the quantitative and qualitative factors used to assess equity compensation proposals. Similar to Institutional Shareholder Services, Inc. ("ISS"), much of the Glass Lewis updates center around broader director or governance related proxy ballot items, as discussed in greater detail below.

US Voting Policy Changes

Compensation Policy Changes

- ***Evaluation of One-Off Awards:*** Specific to sign-on compensation for NEO transition arrangements, Glass Lewis has clarified that sign-on arrangements should be clearly disclosed and accompanied by thorough disclosure regarding the nature of the payments and how they were negotiated. Further, the rationale for any "make-whole" compensation (both the award itself and the amount) should be disclosed. Additionally, for severance or sign-on compensation, Glass Lewis may review the executive's regular target compensation levels or sums paid to other executives (i.e., a predecessor, where appropriate) in evaluating the reasonableness of such arrangements.

  In the context of one-off awards, Glass Lewis also wants to see clarification about how such awards will ultimately affect any regular ongoing compensation arrangements (where applicable). In reviewing the appropriateness of such grants, Glass Lewis evaluates the terms and size of the grants in the context of the company's overall incentive strategy and granting practices, as well as the current operating environment.

  Aon Hewitt Comment: *The Glass Lewis Policy Updates regarding one-off awards is not new, but is instead the formalization of the historical approach to reviewing such awards. The clarification published in these Updates should remind corporate issuers of the need to adequately disclose a sound rationale for such awards (for the award itself and the design and size of the award).*

- ***Evaluation Factors for Equity Compensation Plans:*** Glass Lewis has provided further clarification regarding its approach to equity compensation plans. Specifically, Glass Lewis has added language stating that the evaluation is based on both quantitative and qualitative factors. The qualitative factors include plan administration, method and terms of exercise, expressed or implied rights to reprice, and the presence of evergreen provisions. These are factors that they have already evaluated for years, but have now decided to add specific language to the published guidelines. Similar to the evaluation of one-off awards, the Glass Lewis policy on equity compensation plans, as well as its application has not ultimately changed. Lastly, the guidelines now include a reference that Glass Lewis considers a company's size and operating environment in determining the appropriateness of share requests.

Aon Hewitt Comment: *Similar to the Policy Update for one-off awards, the Glass Lewis Policy Update for equity compensation plans is not new, but is instead the formalization of the historical approach to reviewing such awards. This clarification is likely the result of feedback from issuers and investors alike, as the Glass Lewis approach has historically been perceived as a "black box." Increased visibility as to how Glass Lewis assesses equity compensation plans has been requested by corporate issuers for years.*

Director "Overboarding"

- Beginning in 2017, Glass Lewis will recommend shareholders vote against directors who (a) are executive officers of public companies and serve on more than two boards and (b) non-executive directors who serve on more than five public company boards. This is more restrictive than the current guidelines of three and six, respectively. A grace period for issuers has been provided and voting recommendations for the 2016 proxy season, when Glass Lewis will rely on the previous thresholds.

Aon Hewitt Comment: *Consistent with final policy changes at Institutional Shareholder Services, Inc. ("ISS"), Glass Lewis has published fairly restrictive overboarding requirements. While the grace period before negative vote recommendations will be issued is a welcome addition to the Policies, many directors will likely be surprised at the negative commentary that may be included in the Glass Lewis reports this year if they exceed the new overboarding thresholds.*

Exclusive Forum Provisions (for IPO companies)

- Glass Lewis will no longer automatically vote against the chairman of the nominating and governance committee for IPO companies that include exclusive forum provisions in their governing documents.
- Instead, Glass Lewis will take a case-by-case approach weighing the exclusive forum provision against other bylaw terms that may unduly limit shareholder rights (e.g., supermajority vote requirement, a classified board, and a fee shifting bylaw). This does not change Glass Lewis' stance for the adoption of exclusive forum provisions without shareholder approval outside of spinoff, merger, or IPO situations.

Aon Hewitt Comment: *ISS takes a similar case-by-case approach to exclusive forum provisions. However, we will monitor Glass Lewis's application of this policy to see if they still ultimately automatically vote against certain directors for the inclusion of such provisions in governing documents. While this new Policy affords Glass Lewis more flexibility, it may still ultimately result in a large number of negative vote recommendations for companies adopting these provisions without what Glass Lewis perceives as sufficient justification.*

Nominating Committee Performance

- Glass Lewis has clarified that it may recommend against the chairman of nominating committee for failing to ensure the board has directors with relevant experience, either through periodic director assessment or board refreshment, and this failure has contributed to a company's poor performance.

Aon Hewitt Comment: *This Policy Update should be fairly benign and driven largely by proxy disclosure of board evaluation processes. Assuming that companies disclose adequate board evaluation processes, we do not anticipate that this Policy will result in a material number of negative vote recommendations during the 2016 proxy season.*

Environmental and Social Risk Oversight

- Glass Lewis has codified its view that it may recommend against directors for insufficiently identifying and managing material environmental or social risk. Specifically, Glass Lewis will assess these cases by considering the nature of the risk and the potential effects on shareholder value. Therefore, Glass Lewis views the identification, mitigation and management of environmental and social risks as integral components when evaluating a company's overall risk exposure. Under the new Policy Update, Directors are expected to monitor management's performance in managing and mitigating these environmental and social risks in order to eliminate or minimize the risks to the company and its shareholders. In cases where Glass Lewis has determined that the board or management has failed to sufficiently identify and manage a material environmental or social risk that did or could negatively impact shareholder value, they will recommend shareholders vote against directors responsible for risk oversight in consideration of the nature of the risk and the potential effect on shareholder value.

  Aon Hewitt Comment: *In order to mitigate potential negative scrutiny in this area, issuers in certain industries that could find themselves subject to such Policy application should consider disclosing what (if any) procedures the board and/or relevant committees have in place to evaluate such risks.*

Conflicting Management and Shareholder Proposals on Same Topic

- Glass Lewis has outlined its approach to analyzing and determining which proposal to support when conflicting management and shareholder proposals are presented. In these situations, Glass Lewis will consider:
  - The nature of the underlying issue.
  - The benefit to shareholders from implementation of the proposal.
  - The materiality of the differences between the terms of the shareholder proposal and management proposal.
  - The appropriateness of the provisions in the context of a company's shareholder base, corporate structure, and other relevant circumstances.
  - A company's overall governance profile and, specifically, its responsiveness to shareholders as evidenced by a company's response to previous shareholder proposals and its adoption of progressive shareholder rights provisions.

  Aon Hewitt Comment: *Similar to most of the other Policy Updates, this particular one is the formalization of an already existing policy. Unlike ISS, Glass Lewis does not typically universally support most shareholder proposals, and will in fact, side with management, depending on the factors identified in this list.*

Next Steps

The 2016 Policy Updates are generally minor in nature, except regarding the overboard policy (which is fairly restrictive). Pre-IPO companies should continue to carefully weigh the consequences of decisions that could potentially create harmful market reactions going forward. Other companies should consider board actions, protection of shareholder rights, and the oversight of environmental and social risks going forward per the new clarifications contained within the Policy Updates. Overall, all companies should continue to be wary of poor shareholder optics, shareholder activism, litigation and unwanted media attention in light of both ISS and Glass Lewis influence on proxy ballot items.

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