Director overboarding and cyber risk oversight will be top of mind for Glass Lewis in 2023

December 09, 2022

Glass, Lewis & Co's (Glass Lewis) recently released 2023 Canadian Proxy Voting Guidelines (the Guidelines) include key updates with respect to cyber and climate risk oversight, over-commitment considerations, and the shift to a percentage-based approach to gender diversity. The new and updated policies will apply to shareholder meetings beginning on January 1, 2023.

Takeaways

Directors of Canadian public companies should take note of following Guidelines for the 2023 proxy season:

- Glass Lewis will recommend a withhold vote for the chair of the nominating committee of a board that is not **at least 30 per cent gender diverse**. All members of the nominating committee will receive a negative recommendation where the board has **no gender diverse directors**.
- Directors will be held accountable for **cyber risks and climate-related issues**, and be expected to provide proactive disclosure on the mitigation of such risks.
- Executive officers serving **two public boards of different issuers** may be subject to a negative recommendation from Glass Lewis for overboarding, even if they have not previously received an "against" recommendation on this basis.
- The Guidelines offer clarifications with respect to **multi-class share structures with unequal voting rights**, compensation committee performance and company responsiveness for say-on-pay analysis.
- Updates address a variety of matters relating to executive compensation, including long-term incentive awards, "mega-grants", one-time awards and front-loaded awards.

Cyber risk oversight and director over-commitments among key new policies for upcoming proxy voting season

Board gender diversity

Board gender diversity continues to be an issue of interest for the 2023 proxy season. As noted in our previous bulletin, Glass Lewis has generally recommended a withhold vote for the chair of the nominating committee of TSX issuers' boards counting fewer than two gender diverse directors. For boards of six or less directors, the target was one gender diverse director. Glass Lewis has updated the Guidelines to transition from a fixed numerical target for board gender diversity to a percentage-based approach aligned with ISS' gender diversity policy.

Glass Lewis' board gender diversity policy contemplates not just female representation on the board, but also gender diversity in a broader sense. In particular, "gender diverse directors" are defined in the Guidelines as women and directors that identify with a gender other than male or female.

For issuers listed on the TSX, Glass Lewis will recommend a withhold vote for the chair of the nominating committee of a board that is not **at least 30 per cent gender diverse**, and all members of the nominating committee with no gender diverse directors. Non-TSX listed issuers and issuers with six or fewer directors are expected to have at least one gender diverse director.

A board may be able to mitigate a negative recommendation from Glass Lewis by disclosing a timeline for increasing gender diversity on the board or having a well drafted diversity policy with non-boilerplate language and clear targets. Companies should consider Glass Lewis' percentage-based approach to gender diversity when assessing board composition or filling board vacancies.

Glass Lewis' expectation is consistent with recent corporate trends on board gender diversity. In October 2022, the CSA published the results of its eighth annual review of representation of women on boards and in executive positions. Key highlights include:

- 24 per cent of board seats are held by women;
- The percentage of board vacancies filled by women increased from 35 per cent last year to 45 per cent this year;
- 87 per cent of issuers have at least one woman on their board;
- 30 per cent of issuers have at least three women on their board, an increase of six percent since last year; and
- 7 per cent of issuers have a woman chairing their board.

Environmental and social risk oversight

As ESG remains at the forefront of investors' concerns and regulators, both in Canada and abroad, propose heightened disclosure of climate-related risks, Glass Lewis sees the board's oversight role of environmental and/or social issues as being heightened. While Glass Lewis believes that companies should determine the best structure of their oversight, which can be effectively conducted by specific directors, the entire board, a separate committee, or combined with the responsibility of a key committee, it will generally recommend voting against the governance committee chair of any company in the S&P/TSX Composite which fails to provide explicit **disclosure concerning board-level oversight on environmental and/or social issues**.

In terms of climate-related issues, Glass Lewis will also hold directors accountable for climate-related issues and expect clear and comprehensive **disclosure on climate risks**

and mitigation thereof, especially from companies whose greenhouse gas emissions represent a financially material risk. Glass Lewis may therefore recommend voting against a responsible director where companies with increased climate risk exposure (such as those companies identified by groups including Climate Action 100+) have not provided thorough Task Force on Climate-related Financial Disclosures-aligned climate-related disclosure, or have not defined board oversight responsibilities for climate-related issues in enough detail.

This new requirement is consistent with the climate-related disclosure requirements contained in the proposed National Instrument 51-107 - Disclosure of Climate-related *Matters* and its companion policy (the Proposed Instrument), which would apply to all reporting issuers other than investment funds. Currently, the Proposed Instrument is still under evaluation by the CSA. Please refer to our previous bulletin for more information.

Cyber risk oversight

As cyber attacks continue to pose a threat to consumers, companies and national security, Glass Lewis has introduced new guidance on board oversight of cyber risk, which it views as a material issue for all companies to mitigate. Although Glass Lewis will generally not make recommendations based on cyber-related oversight or disclosure, it will closely evaluate such disclosure where cyber breaches have caused significant harm to shareholders and may recommend against appropriate directors where such disclosure is insufficient. Glass Lewis believes appropriate disclosure can assist shareholders understand the seriousness with which companies consider cyber security issues.

Director commitments

In prior years, Glass Lewis would recommend that shareholders vote against a director serving as an executive officer of any public company while serving on more than two public company boards and any other director serving on more than five public company boards. Starting in 2023, Glass Lewis will generally advise opposing the election of any TSX company director who is:

- an **executive officer** of a public company while serving on **more than one additional external public company board**;
- an **executive chair or vice chair** of a public company while serving on **more than two additional external public company boards**; or
- a **non-executive director** on **more than five public company boards** in total.

The director commitment policies above would not apply to directors who serve as an executive officer of a public company and on up to five TSXV boards, or any non-executive director who serves on up to nine venture boards.

Glass Lewis may consider the following factors in determining whether a director has sufficient time to devote to its board responsibilities and therefore whether to recommend voting against a director for overboarding:

- the size and location of the other companies where the director serves on the board;

- the director's board roles at the companies in question;
- whether the director serves on the board of any large privately-held companies;
- the director's tenure on the boards in question; and
- the director's attendance record at all companies.

Glass Lewis may refrain from making a negative recommendation if the company provides sufficient rationale for their continued board service. If the director in question serves on boards within a consolidated group of companies in related industries, or represents a firm with the sole purpose of managing a portfolio of investments including the company, Glass Lewis will generally refrain from providing a negative recommendation but still expects issuers to proactively address shareholder concerns with respect to director commitment level.

Multi-class share structures with unequal voting rights

Last year, Glass Lewis began recommending voting against the chair of the governance committee of companies with multi-class share structures and unequal voting rights that do not provide a reasonable sunset clause (generally seven years or less). For 2023, Glass Lewis may instead consider recommending voting against a representative of the multi-class shareholder in cases where it deems more appropriate to hold the multi-class shareholder accountable. Directors may also avoid a negative recommendation on this basis where the company has multi-year evidence of recent exemplary governance practices and responsiveness to shareholders.

Company responsiveness for say-on-pay analysis

In Canada, say-on-pay resolutions are not yet mandated for all reporting issuers. However, say-on-pay resolutions generally receive very strong support. According to Institutional Shareholder Services' proxy voting guidelines published in December 2021, the average say-on-pay support level in Canada has been over 90 per cent in the last five years. The Canadian Coalition for Good Governance recommended in its comment letter dated March 31, 2021 on the proposed Bill C-97 regulations that where a say-on-pay vote receives low shareholder support (typically less than 80 per cent), the board should report back within a reasonable time on its engagement efforts to understand shareholder concerns. Glass Lewis shares a similar approach. When assessing the support levels of a company's previous say-on-pay votes, Glass Lewis will scrutinize the level of opposition among disinterested shareholders and expect companies to demonstrate a commensurate level of engagement and responsiveness to shareholder concerns. In terms of robust disclosure, Glass Lewis will look for companies to provide a discussion of rationale for not implementing changes to pay decisions that drove low support and intention going forward.

Executive compensation matters

Glass Lewis has also updated the Guidelines to address a variety of matters relating to executive compensation, including:

- *Long-term incentive awards*: Glass Lewis will expect the minimum percentage of the long-term incentive grant that is performance-based to be 50 per cent (33 per cent in previous years' guidance). As of 2023, Glass Lewis will raise concerns in its analysis with executive pay programs providing less than half of an executive's long-term incentive awards that are subject to performance-based vesting conditions. Glass Lewis may refrain from a negative recommendation in the absence of other issues with the program's design and operation, but will take issue with a negative trajectory in the allocation amount.

- *Mega-grants:* Glass Lewis will recommend voting against the chair of the compensation committee when outsize awards (so called "mega-grants") have been granted and the awards raise concerns such as excessive quantum, lack of sufficient performance conditions, and/or are excessively dilutive.
- *One-time awards:* Glass Lewis has clarified that reasonable disclosure about one-time awards should include a discussion surrounding the determination of quantum and structure for such awards.
- *Compensation committee discretion on incentive payouts:* Glass Lewis has codified its view on certain exercise of compensation committee discretion on incentive payouts. Companies should provide thorough discussion of the impact of significant events not otherwise captured in the performance metrics of an incentive program on the committee's decision to exercise discretion or refrain from exercising discretion over incentive pay outcomes.
- *Front-loaded awards*: Glass Lewis notes that the use of front-loaded awards may raises concerns as to the increased restraint placed upon the board to respond to unforeseen factors.

Next Steps

As the 2023 proxy season is fast approaching, we encourage you to contact BLG if you have questions related to the Glass Lewis Guidelines, or for more information on any other corporate governance initiatives. You may also contact the authors of this article or any of the key contacts noted below.

By

Philippe Tardif, Laura Levine, Jennifer Jiang, Emma Ouellet Lizotte

Expertise

Capital Markets, Corporate Governance

BLG | Canada’s Law Firm

As the largest, truly full-service Canadian law firm, Borden Ladner Gervais LLP (BLG) delivers practical legal advice for domestic and international clients across more practices and industries than any Canadian firm. With over 725 lawyers, intellectual property agents and other professionals, BLG serves the legal needs of businesses and institutions across Canada and beyond – from M&A and capital markets, to disputes, financing, and trademark & patent registration.

blg.com

BLG Offices

Calgary

Centennial Place, East Tower
520 3rd Avenue S.W.
Calgary, AB, Canada
T2P 0R3

T 403.232.9500
F 403.266.1395

Ottawa

World Exchange Plaza
100 Queen Street
Ottawa, ON, Canada
K1P 1J9

T 613.237.5160
F 613.230.8842

Vancouver

1200 Waterfront Centre
200 Burrard Street
Vancouver, BC, Canada
V7X 1T2

T 604.687.5744
F 604.687.1415

Montréal

1000 De La Gauchetière Street West
Suite 900
Montréal, QC, Canada
H3B 5H4

T 514.954.2555
F 514.879.9015

Toronto

Bay Adelaide Centre, East Tower
22 Adelaide Street West
Toronto, ON, Canada
M5H 4E3

T 416.367.6000
F 416.367.6749