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## ISS 2022 Benchmark Policy Consultation

On Nov. 4, 2021, influential proxy advisory firm Institutional Shareholder Services Inc. (“ISS”) released proposed updates to its main benchmark proxy voting policies in multiple regions, including Canada and the U.S. It is seeking comment from market participants until Nov. 16 at 5 p.m. ET. We encourage our clients to review the proposed changes and consider submitting their feedback to ISS on areas that matter to their business. Those who wish to share their thoughts are asked to e-mail ISS at [policy@issgovernance.com](mailto:policy@issgovernance.com).

For the North American markets, ISS is soliciting comments on policies related to board diversity, board responsiveness, the Say-on-Climate movement, unequal voting rights and board accountability related to climate change. **Most interestingly, we note that ISS is contemplating a shift in its proxy voting policies in the U.S. that would take aim at unequal voting rights at all U.S. companies and would see ISS recommend opposing the election of the responsible directors.** By targeting multi-class voting structures, ISS says it seeks to address “the problematic governance provision most adverse to shareholders’ rights.”<sup>1</sup>

If adopted for U.S. issuers, this policy will come into effect in Feb. 2023 following a one-year grace period. In its Nov. 4 publication, ISS warns that the policy will see it recommend shareholders vote against the election of directors at “many large or iconic U.S. companies” that have unequal voting structures, with some noted exceptions. As an example, ISS explicitly names a handful of well-known U.S. companies whose directors will likely be targeted by this policy, assuming the status quo: Alphabet Inc., Meta Platforms Inc. (formerly Facebook Inc.), Ford Motor Company, Berkshire Hathaway Inc. and The New York Times Company.

The proposed policy change south of the border on unequal voting rights raises questions as to whether the Canadian market will be next.

ISS said it will finalize and publish its final benchmark policy changes by or around late November 2021. It is important for public companies to closely monitor the evolution of the proxy advisors’ voting policies because their recommendations inform and guide the voting practices of many institutional shareholders.

Below is a summary of the policy changes being contemplated by ISS for the Canadian and U.S. markets:

### Canada

#### Board Gender Diversity

The board gender diversity policy that ISS previously announced in 2021 will apply in 2022, with some updates. It specifies that if women comprise less than 30% of a board of an S&P/TSX Composite issuer, the company should have a formal commitment to achieve the 30% female representation target before or at its 2023 AGM. When a company does not comply, ISS will generally recommend that shareholders withhold

<sup>1</sup> [Proposed Benchmark Policy Changes for 2022: Request for Comments](#). Institutional Shareholder Services. Published on Nov. 4, 2021.

their votes for the Chair of the Nominating committee or Chair of the Board if no nominating committee or chair has been identified. Directors may also come under scrutiny by ISS at Toronto Stock Exchange-listed companies that are not in the Composite Index when such a company has not disclosed a formal written gender diversity policy and has no female directors.

If these deficiencies on the boards of Composite or non-Composite TSX companies persist for two or more years, ISS will evaluate on a case-by-case basis whether a withhold recommendation is warranted for additional directors. ISS is looking to tighten its policy that currently affords companies the opportunity to adopt a gender diversity policy that includes measurable goals and/or targets “within a reasonable period of time.” The proposed revision to the policy would require companies make a firm commitment to increasing board gender diversity at or prior to the next AGM.

**Rationale:** ISS' Gender Diversity Policy was first introduced in Canada in 2018. It initially targeted companies in the S&P/TSX Composite Index and was expanded in 2019 to include all widely held TSX companies, which was defined by ISS based on the number of ISS clients holding securities of a company. Based on recent ISS data, TSX-listed company boards with no female directors now appear to be outliers. As such, the gender diversity policy for widely held non-S&P/TSX Composite Index companies is being expanded to include the entire TSX-listed universe.

### **Advisory Vote on Executive Compensation (Say-on-Pay) Management Proposals - Board Communications and Responsiveness**

Under the current Canadian policy, ISS will evaluate board responsiveness in instances where a company's previous Say-on-Pay proposal received the support of less than 70% of votes cast. ISS is proposing to increase that threshold to 80% based on Canadian market expectations.

**Rationale:** Such a move would align ISS with Glass Lewis & Co. LLC's policy for board responsiveness, as well as the expectations of the Canadian Coalition for Good Governance (CCGG). In Canada, Say-on-Pay resolutions are not yet mandated for all reporting issuers and, according to ISS, roughly 30% of the TSX issuers under ISS coverage currently provide Say-on-Pay resolutions. These resolutions generally receive very strong support, with the average support level in Canada being more than 90% in the last five years.

## **All Markets**

### **Say-on-Climate (SOC) Management Proposals**

ISS is seeking to codify a framework for analyzing management proposals for climate transition plans. It intends to consider proposals on a case-by-case basis and says it will weigh 10 different factors in its review, including the extent to which a company's climate-related disclosures are aligned with the parameters set by the Task Force on Climate-Related Financial Disclosures (TCFD), as well as the quality of the disclosure of a company's supply chain and operational Greenhouse Gas (GHG) emissions (Scopes 1, 2 and 3).

**Rationale:** In 2021 to date, there have been 25 management Say-on-Climate proposals globally, as per ISS. The proposals were in the following countries: Canada (1); France (3); South Africa (3); Spain (4); Switzerland (1); the U.K. (10); the U.S. (2); and Australia (1). This proposed policy update will document the thought process that ISS has been employing to review such proposals in a bid to provide transparency to the market and incorporate feedback received from investors in ISS' [Climate Survey results](#).

### **Say-on-Climate (SOC) Shareholder Proposals**

Similarly, ISS is adding a policy for reviewing Say-on-Climate shareholder proposals that will assess each request on a case-by-case basis. In its process, ISS will consider four factors, including the completeness of

a company's climate-related disclosures and whether the company has been the subject of recent controversies related to its GHG emissions.

**Rationale:** Say-on-Climate shareholder proposals emerged late in 2020 and increased in frequency in 2021. They generally ask companies to publish a climate action plan and to put these plans to a regular shareholder vote on a non-binding basis. Similar to SOC management proposals, this proposed policy will provide a transparent framework allowing for consistency across markets.

## United States

### Board Diversity

For annual meetings on or after Feb. 1, 2023, ISS is proposing to apply its expectation that a public company board should contain at least one female director to most listed U.S. companies, from the current universe of issuers in the Russell 3000 and S&P 1500 indices.

On racial and ethnic board diversity, we note that the ISS policy announced last year for U.S. companies in the Russell 3000 and S&P 1500 indices to have at least one racially/ethnically diverse director will go into effect in 2022 after the one-year grace period in 2021.

**Rationale:** ISS adopted a U.S. board gender diversity policy in 2019, which went into effect in Feb. 2020 for companies in the Russell 3000 or S&P 1500 indices. ISS notes that many investors continue to express an interest in seeing increased levels of gender diversity on corporate boards.

### Unequal Voting Rights

As mentioned above, ISS is proposing to target directors at companies with multi-class common share structures on the basis of the philosophical principle that one share should carry one vote. Starting Feb. 1, 2023, the proposed change would see ISS generally vote withhold or against directors individually, committee members or the entire board (except new nominees) if a U.S. company employs a common stock structure with unequal voting rights, regardless of when the company went public.

ISS said exceptions to this policy will generally be limited to:

- Newly listed public companies with a sunset provision of no more than seven years from the date of going public,
- Limited partnerships and the operating partnerships unit structure of REITs,
- Situations where unequal voting rights are considered de minimis, or
- The company provides sufficient protections for minority shareholders, such as allowing minority shareholders a regular binding vote on whether the capital structure should be maintained.

ISS notes that its current U.S. policy for companies that go public with a multi-class structure with unequal voting rights includes recommendations against all nominees. Among several questions posed to market participants, ISS is asking which directors should be targeted and whether any types of unequal voting structures should be excluded from the policy.

In the same vein, ISS is proposing that newly public companies with unequal voting rights will warrant a continued vote against certain directors in subsequent years unless the problematic capital structure is reversed, removed or subject to a newly added reasonable sunset. No sunset period of more than seven years from the date of the IPO will be considered to be reasonable.

**Rationale:** ISS notes that companies are continuing to maintain and go public with adverse governance provisions. Therefore, it is seeking to enhance its policies for all U.S. companies in the name of shareholder democracy, beginning with multi-class voting rights:

“Due to the strong support expressed through the survey results and roundtable discussions, ISS is commencing with the removal of the grandfathering of companies with poor governance, focusing first on unequal voting rights, which is considered the problematic governance provision most adverse to shareholders' rights.”

Based on the above, we expect ISS to contemplate targeting other adverse governance practices at U.S. companies, such as the use of supermajority vote requirements to amend governing documents and a classified board structure, in future policy updates.

### **Board Accountability & Climate**

Proposed ISS benchmark policy changes for 2022 will include the assessment of and focus on the world's highest GHG emitting companies. In several major markets including the U.S. but excluding Canada, ISS is proposing to introduce recommendations to vote against the re-election of relevant directors or any other appropriate items at companies that have not made appropriate climate-related disclosures, such as according to the TCFD framework, or that have not set quantitative GHG reduction targets.

**Rationale:** ISS is proposing a new climate-related board accountability policy based on what it refers to as widely held investor expectations of the steps that should be taken by these companies to assess, mitigate and report on their climate change risks and targets.

If you have any questions about this update or to seek assistance with your company's submission to ISS, please feel free to contact Kingsdale's experts listed below to discuss directly.

*This client advisory has been prepared by the Governance Advisory team at Kingsdale Advisors.*

**Kelly Gorman**  
Executive Vice President  
Governance Advisory  
(647) 289-5226  
kgorman@kingsdaleadvisors.com

**Anqi Xu**  
Vice President  
Governance Advisory  
(647) 995-4999  
axu@kingsdaleadvisors.com

**Christina Pellegrini**  
Associate Director  
Governance Advisory  
(416) 726-4505  
cpellegrini@kingsdaleadvisors.com