



CLIENT ALERT

Navigating Compensation Governance

Summary of Key ISS and Glass Lewis 2024 Canadian Policy Updates

ISS released a preview of updates to its Canadian policies, with one change related to governance and none related to compensation. Glass Lewis also recently released its Canadian [2024 Policy Updates](#), which were more extensive and impact executive compensation and governance.

Summarized below are highlights of these ISS and Glass Lewis updates and Meridian's commentary.

ISS 2024 Policy Updates

Board Racial and Ethnic Diversity: S&P/TSX Composite companies will be expected to have at least one racially or ethnically diverse director on the ballot for AGMs on or after February 1, 2024. In the absence of this diversity, ISS will generally vote against or withhold from the Chair of the Nominating Committee (or equivalent/Board Chair). ISS may elect not to recommend withhold if the company has provided a formal, publicly-disclosed written commitment to add at least one racially or ethnically diverse director by the next AGM.

Meridian Comment: This policy was announced in 2022 and has been phased in with an effective date of February 1, 2024. The policy is a bright line test, similar to the policy on gender diversity. This change aligns with the views of many Canadian institutional investors, who note in their own voting policies that they will withhold votes for the Nominating Committee Chair where there is no clear ethnic or racial diversity on the Board.

Glass Lewis 2024 Policy Updates

Compensation-Related Policy Updates

Clawback Provisions: Glass Lewis has indicated that clawback provisions should include the ability to recoup incentive compensation where there is bad behaviour whether or not it results in a restatement of financial statements. Glass Lewis identifies bad behaviour as including: material misconduct; material reputational failure; material risk management failure; or material operational failure, which has not already been reflected in incentive payments. The scope of a company's clawback provisions may be a qualitative factor in Glass Lewis' Say-on-Pay analysis.

Meridian Comment: Currently, many Canadian clawback policies provide for recoupment only if there has been misconduct that has resulted in a restatement of the company's financial statements. Many companies have delayed reviewing their clawback policies, pending the final implementation of the Dodd-Frank clawback rules, which apply to all U.S. listed companies (including Canadian companies that are U.S. foreign private issuers). We expect many companies to review their clawback policies now these rules are in-force. We expect some companies will add provisions for recoupment based on misconduct and reputational risk, even when this does

not result in a restatement of financials. Recent high-profile scandals like McDonald's CEO misconduct have increased pressure on Boards to re-assess tools for recoupment and we think this updated guidance from Glass Lewis will be a further catalyst for more comprehensive review of policies relative to market and best practice.

Executive Share Ownership Guidelines: Glass Lewis added a new section to its policy with expectations for executive share ownership requirements and for clear disclosure of guidelines in the CD&A. Glass Lewis comments that unearned performance-based awards and/or unexercised options should not count towards compliance absent a cogent rationale. A company's executive share ownership guideline design may be a qualitative factor in Glass Lewis' Say-on-Pay analysis.

Meridian Comment: Glass Lewis' view on what "should count" for towards share ownership requirements generally aligns with market practice. Few companies count the in-the-money value of stock options and a minority of companies count unearned performance-vested awards towards ownership. Where companies do count unearned PSUs, this is typically because they reflect a material part of the long-term incentive program. The main difference between Glass Lewis' view and the Canadian Coalition for Good Governance (CCGG)'s view is that Glass Lewis does not object to counting unvested restricted (time-based) share units, whereas CCGG would like to see ownership met by common shares.

Non-GAAP Incentive Metrics: Glass Lewis expects companies that use non-GAAP incentive metrics to disclose a reconciliation to GAAP (or IFRS in Canada). Failure to include this disclosure will impact the assessment of the quality of executive pay disclosure and may be a factor in Glass Lewis' recommendation on Say-on-Pay.

Meridian Comment: Many companies use non-IFRS incentive metrics in their incentive plans, generally to exclude line items outside management's ability to control (and to focus management on the things they can control). We do not expect companies to move away from these metrics, but that they will face increased pressure to more fully disclose, reconcile, and explain in the proxy the rationale for the differences between incentive metric definitions and IFRS definitions.

Director-Related Policy Updates

Human Capital Management: Where a board has failed to respond to legitimate concerns with a company's human capital management practices, Glass Lewis may recommend voting against the Chair of the Committee tasked with oversight of the company's environmental and/or social issues, the Chair of the Governance Committee or the Chair of the Board, as applicable.

ESG-Related Policy Updates

Board Accountability for Climate-Related Issues: Glass Lewis expects companies with material exposure to climate risk from their own operations to provide climate-related disclosure in line with the recommendations of the Task Force on Climate-related Financial Disclosures and to have explicit and clearly defined Board oversight responsibilities for climate-related issues. Where either of these disclosures is lacking, Glass Lewis may recommend against the responsible directors, or the Chair of the Governance Committee. Beginning in 2024, Glass Lewis will apply this policy to TSX 60 companies operating in industries where the Sustainability Accounting Standards Board has determined that the companies' GHG emissions represent a financially material risk.

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