

Key Changes in Proxy Voting Guidelines for 2019

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Both ISS and Glass Lewis have recently updated their proxy voting guidelines, featuring key changes that could affect shareholder voting habits in 2019.

Changing policies to reflect changing times

Leading corporate governance service providers Institutional Shareholder Services Inc. ("ISS") and Glass Lewis have updated their worldwide proxy voting guidelines for 2019, including for shareholders of UK companies.

The updates generally reflect current trends in corporate governance, as well as changes to the wider regulatory framework. These updates will affect the voting patterns of many institutional and passive investors, who are increasingly utilising the benchmark guidelines to determine their block votes at shareholder meetings. With this in mind, the updated guidelines have the potential to influence voting behaviour on a wide range of corporate governance issues, including board composition, corporate culture and social and environmental concerns.

Importantly, the updated proxy voting guidelines reflect the changing nature of proxy voting and the way in which proxy advisers determine and deliver their voting recommendations. For example, a number of the updated guidelines enable proxy advisers to undertake a more subjective, qualitative assessment of a company's processes and performance. This shift opens the door for proxy advisers to increase their influence in the market, and equally reflects a wider move towards more succinct and precise corporate governance reporting in general.

"The policy changes we are announcing today have been carefully considered and are designed to underpin the needs of our institutional investor clients for informed and relevant research and recommendations based on widely recognized good standards of, and approaches to, corporate governance."

Georgina Marshall, Global Head of Research and Chair of the ISS Global Policy Board

ISS 2019 Proxy Voting Guidelines updates

List of the key changes to the ISS Proxy Voting Guidelines

External auditors

- In recommending a vote in favour of the appointment of external auditors, ISS will consider (i) if there are concerns around the effectiveness of the auditors (not just the procedures used by the auditor) and (ii) if the lead audit partner has been linked with a significant auditing controversy.

Election of Directors

- ISS will recommend against the re/election of directors where egregious actions related to the director's service on other boards raise substantial doubt about that director's ability to effectively oversee management and serve in the best interests of shareholders at any company.

Remuneration policy

- Subject also to other considerations, voting shall generally be in favour of annual bonuses as long as they are typically set at no more than 50% of the maximum bonus potential and any pay out above this level is supported by a sufficiently robust explanation.
- Furthermore, ISS continues to refer to the Investment Association Principles in considering its recommendations in connection with LTIPs. ISS continues to encourage performance periods that are longer than three years, and now makes clear that share awards should be subject to a vesting and holding period of five years or more. This requirement also reflects the recommendations set out in the updated UK Corporate Governance Code earlier this year (which is effective from 1 January 2019) (the "New Code").

Remuneration report

- In instances where there has been a material decline in a company's share price, remuneration committees should consider reducing the size of Long-Term Investment Plans (LTIPs) awards at the time of the grant. ISS's rationale for this change is that remuneration committees should be actively considering award sizes on an annual basis, particularly where there has been significant volatility in the share price.
- Fees paid to non-executive directors should not be excessive in relation to other similar sized businesses in the same sector.

Authorise Issue of Equity with and without Pre-emptive Rights

- A recommendation to vote against an issuance of equity may now be based on a company's compliance with the Pre-emption Group Principles in general and at any time (rather than restricted to non-compliance in the previous financial year with respect to a particular authorisation). Furthermore, a recommendation to vote against an equity issue may be applied to all share issuance authorities, not just the disapplication of pre-emption rights.

Environmental and Social Issues

- ISS has now clarified the factors it will examine (on a case-by-case basis) when recommending a vote on different environmental and social issues. One new factor that ISS will examine when reviewing shareholder proposals is whether there are significant controversies, fines, penalties or litigation associated with the company's environmental or social practices.

The ISS updates shall be effective for general meetings on or after 1 February 2019

Glass Lewis 2019 Proxy Voting Guidelines updates

List of the key changes to the Glass Lewis Proxy Paper Guidelines 2019

Board skills and diversity

- Glass Lewis clarifies the expectation that FTSE 100 companies provide meaningful disclosure in relation to board members' required skills and diverse backgrounds. In addition, when assessing board diversity concerns, Glass Lewis will now take into account a company's disclosed gender pay gap data and the composition of the company's executive pipeline for larger companies.

Board and Committee responsiveness

- Where appropriate, when 20% of the shareholders of a company vote contrary to a management recommendation, Glass Lewis may now hold chairs and members of the relevant committees accountable

by recommending voting against their re-election in circumstances where shareholder concerns have not been adequately addressed.

Environmental and Social Risk Oversight

- Where it is clear that a company has not properly managed or mitigated environmental or social risks to the detriment of shareholder value, or when such mismanagement has threatened shareholder value, Glass Lewis may consider recommending that shareholders vote against members of the board (or relevant members of the audit and/or risk committee) who are responsible for the oversight of environmental and social risks.

Pay ratios

- Glass Lewis have updated their guidelines to reflect legislation passed in July 2018 requiring UK quoted companies with over 250 employees to publish the pay ratio between their CEO and average UK employee. They have confirmed that, at present, this will not be a determinative factor in their voting recommendations.

These changes reflect the key updates to the Glass Lewis guidelines for 2019.

Following the recent updates to these guidelines, and the release of the New Code, it appears that corporate governance is once again shaping up to be a hot topic in 2019.

For more information, please reach out to your White and Case contact.

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