Harvard Law School Forum on Corporate Governance

Annual Meeting and Corporate Governance Trends in 2023

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Consider New DGCL Amendments Permitting Officer Exculpation

Effective August 1, 2022, Section 102(b)(7) of the Delaware General Corporation Law (DGCL) was amended to authorize exculpation of certain senior officers of Delaware corporations from personal liability for monetary damages in connection with breaches of their fiduciary duty of care (the Officer Exculpation Amendment).

Explanation of the Officer Exculpation Amendment

Since its original adoption in 1986, Section 102(b)(7) of the DGCL has authorized exculpation of directors of Delaware corporations from personal liability for monetary damages in connection with breaches of their fiduciary duty of care. However, until the recent enactment of the Officer Exculpation Amendment, officers of Delaware corporations were not afforded the same protection — despite often having overlapping roles and, in recent years, being susceptible to similar lawsuits. The Officer Exculpation Amendment reduces the differential treatment between directors and officers, but Section 102(b)(7) imposes additional limitations on exculpating senior officers from liability.

Now Delaware corporations may include provisions in their certificates of incorporation that limit or eliminate the personal liability of certain enumerated officers.[1] As is the case with director exculpation, officer exculpation is limited to instances in which a breach of the fiduciary duty of care has occurred. Exculpation from liability is not available under the DGCL to directors or officers for breaches of their duty of loyalty or for "acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of the law," among other exclusions.

[1] These enumerated officers include persons who at the time of an act of omission to which liability is asserted are deemed to have consented to service by the delivery of process to the registered agent of the corporation pursuant to Section 3114(b) of the DGCL. This includes any person who (i) is or was the president, chief executive officer, chief operating officer, chief financial officer, chief legal officer, controller, treasurer or chief accounting officer of the corporation, (ii) is or was identified in the corporation's Summary Compensation Table included in the corporation's proxy statement or annual report on the corporation's Form 10-K or (iii) has, by written agreement with the corporation, consented to be identified as an officer for purposes of accepting service of process.

An important difference between officer and director exculpation under the DGCL is that officer exculpation is not permitted in connection with claims brought by or in the right of the corporation, including stockholder derivative claims, while director exculpation under the DGCL is not subject to that limitation.

In order to afford senior officers with the protection from personal liability afforded by exculpation under Section 102(b)(7), Delaware corporations must "opt in" to the law's coverage by including an exculpation clause in their original certificates of incorporation or by adopting an amendment to their certificates of incorporation.[2] Pursuant to Section 242(b) of the DGCL, in order to amend a corporation's certificate of incorporation, its board of directors must approve the amendment, declare its advisability and submit the amendment to a vote of stockholders at an annual or special meeting of stockholders. Adoption of such amendment requires the affirmative vote of holders of a majority of the outstanding shares of stock entitled to vote on the proposed amendment (unless a greater number of votes, or any separate class or series of votes, is required to amend the corporation's certificate of incorporation pursuant to the terms thereof).[3]

Proxy Advisor Response

Although the Officer Exculpation Amendment was adopted just several months ago, at least eleven corporations have filed proxy statements in that time seeking stockholder approval to amend their certificates of incorporation to include an officer exculpation clause. Although preliminary indications suggest that ISS and Glass Lewis have viewed officer exculpation amendments as generally acceptable, as described below, that may not be the case for Glass Lewis in all cases going forward. In issuing voting recommendations to date, neither ISS nor Glass Lewis has expressed any material concerns or made any adverse voting recommendations specifically addressing officer exculpation proposals (or made adverse voting recommendations in the reelection of directors who have approved such exculpation proposals).

The first two publicly filed proxy statements seeking stockholder approval of officer exculpation amendments were put forth as part of a "bundled" package proposal where stockholders were asked to vote either "for" or "against" a number of changes to the corporations' certificates of incorporation in their entirety, rather than on each individual amendment. In both instances, ISS and Glass Lewis did not explicitly take a position with respect to the officer exculpation amendment, focusing instead on the aggregate impact of the "bundled" amendments on stockholder rights. In one instance, Glass Lewis recommended a vote "against" the proposal bundling amendments to the certificate of incorporation, noting that the practice of bundling several amendments into a single proposal "negatively impacts the ability of shareholders to judge each amendment on its own merits."

Nine corporations have subsequently put forth stand-alone proposals to amend the certificate of incorporation to include officer exculpation provisions. Of those nine, proxy advisor recommendations are available in six instances as of the date of this writing, and in all six cases,

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[2] A proposal to amend the certificate of incorporation to include officer exculpation will require a preliminary proxy filing. Companies should consider and incorporate such preliminary proxy filing in their timelines for their 2023 annual meeting filings.

[3] In two instances, the corporations' stockholders failed to approve the officer exculpation amendment, due primarily to each corporation having a supermajority voting requirement and a significant number of retail stockholders that did not vote on the amendment proposal.

both ISS and Glass Lewis have specifically recommended that stockholders vote "for" the officer exculpation amendments. Glass Lewis noted that such amendments will not "have a negative impact on shareholders" and ISS echoed this outlook.

These favorable recommendations highlight the importance of separating proposals for stockholder approval of officer exculpation clauses from other proposals to enhance the likelihood that such proposals receive a favorable recommendation and ultimately obtain stockholder approval.

On November 4, 2022, ISS proposed amendments to its benchmark voting policy for 2023 to "[g]enerally vote for proposals providing for exculpation provisions in a company's charter to the extent permitted under applicable state law." ISS cited the Officer Exculpation Amendment as the rationale for this proposed policy update. ISS is expected to publish its final policy updates for the coming year in December 2022, although final updates commonly vary from the proposed updates.

Despite its lack of adverse voting recommendations on officer exculpation proposals thus far, Glass Lewis' recently adopted 2023 policy guidelines, which are effective for annual meetings in 2023, state that Glass Lewis "will closely evaluate proposals to adopt officer exculpation provisions on a case-by-case basis [and] generally recommend voting against [officer exculpation] proposals eliminating monetary liability for breaches of the duty of care for certain corporate officers, unless compelling rationale for the adoption is provided by the board, and the provisions are reasonable."

Additional Legal Considerations

To date, two separate complaints have been filed in Delaware Chancery Court challenging the adoption by two separate issuers of an amendment to their certificates of incorporation implementing an officer exculpation clause. Both lawsuits relate to whether a class of nonvoting shares is entitled to vote on officer exculpation amendments and seek to invalidate the amendment.

Next Step: Proposing and Adopting a Certificate of Incorporation Amendment

Corporations wishing to adopt an amendment to their certificates of incorporation to include officer exculpation should consult counsel to consider the related requirements, legal considerations and implications involved. Corporations should also consider working with counsel to conduct a holistic governance review to ensure their governing documents align with the most recent market standards and trends and with those of their peers.

Consider Universal Proxy Rules

In November 2021, the SEC adopted amendments to the proxy rules to mandate that companies use universal proxy cards in contested elections, which permit shareholders to "mix and match" from competing slates of candidates without having to attend the shareholder meeting.[4] Under

[4] See our November 19, 2021, client alert "SEC Mandates Universal Proxy Cards in Election Contests."

the new rules, companies and dissidents must list on their proxy cards all duly nominated director candidates, including the board's nominees, any dissident's nominees and any proxy access nominees.[5] Previously, shareholders generally had to choose between voting for the company's slate on the company's proxy card or the activist's slate on the activist's proxy card.

Key Action Items

Companies should address the following matters:

Nominee consent. Director nominees must consent to be named in any proxy statement — not just the company's — relating to the shareholder meeting at which directors will be elected. Companies should consider revising the consent language in their bylaw provisions regarding advance notice and proxy access and their D&O questionnaires to ensure that nominees are required to give the necessary consents.

Notice. A dissident shareholder seeking to run an election contest is required to provide notice to the company not later than 60 calendar days prior to the anniversary date[6] of the previous year's annual meeting. This notice requirement is in addition to any notice or other requirements in a company's governing documents, and generally the SEC notice requirement is later than the notice required under a company's advance notice bylaws. Companies without an advance notice bylaw should consider adopting one, and companies with a bylaw that provides for a notice period of 60 days or less in advance of the anniversary of the meeting date may want to consider amending the bylaw to provide for additional notice.

In addition, a company receiving a notice from a dissident is required to notify the dissident of the names of the company's nominees no later than 50 calendar days prior to the anniversary date of the previous year's annual meeting.

Dissident proxy statements. A dissident must file its definitive proxy statement at least 25 calendar days before the shareholder meeting or five calendar days after the company files its definitive proxy statement, whichever is later, and include disclosure concerning the dissident's intent to solicit holders of at least 67% of the voting power entitled to vote in the election of directors. A dissident's failure to timely file its proxy statement will preclude it from soliciting proxies, and the company has the option to disseminate a new proxy card with only the company's nominees (and, if applicable, any proxy access nominees).

Company proxy statements. Companies must disclose in their proxy statements — for contested and uncontested elections — the deadline for receiving notice of a dissident's nominees under the universal proxy rules.

Company and dissident proxy cards. The proxy cards for a contested election that companies and dissidents are required to provide shareholders must:

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[5] The new rules do not apply to elections held by registered investment companies and business development companies.

[6] There is a provision for adjusting the deadline if there was no previous annual meeting or the date of the meeting has changed by more than 30 days from the previous year. This adjustment is also applicable to the related notice requirement imposed on companies.

- list the names of all duly nominated nominees, clearly distinguishing between company nominees, dissident nominees and proxy access nominees, alphabetically listing the nominees within each group;
- use the same font type, style and size for all nominees presented on the card;
- prominently disclose the maximum number of nominees for which authority to vote can be granted; and
- prominently disclose how a proxy will be treated if it is cast for more or less than the number of directors to be elected, or if the proxy does not provide a direction.

Bylaw amendments. The universal proxy rules do not contain an enforcement mechanism for a dissident's failure to comply. Accordingly, companies should consider amending their bylaws so that failure to comply with these rules renders a dissident's nominees ineligible for election under the bylaws.

Potential Impact of the Universal Proxy Rules

The impact of mandated universal proxy cards is unclear. Potential impacts, however, include the following:

- Because shareholders can more easily vote for a mix of company and dissident nominees, activists may be more likely to win at least one board seat in a contested election.
- Given the focus on individual nominees, as opposed to management and dissident slates as a whole, management's individual nominees may be more closely scrutinized.
- Proxy advisors may begin issuing recommendations supporting a mix of candidates from management and dissident slates.
- "Nominal" proxy contests — in which dissidents incur minimal costs to pursue a contest with no intention of gaining a board seat, such as to gain leverage in negotiations with the company — may increase.

Companies should evaluate their proxy disclosure to ensure they are effectively conveying the skills and attributes that each of their nominees bring to the board room.

Revisit Board Leadership and Risk Oversight Disclosures

Recent SEC staff comment letters have requested enhanced proxy statement disclosures by companies regarding board leadership structure and risk oversight. The staff has issued comments to a cross section of companies from different industries, without regard to the leadership structure selected by the company. The staff issued a different mix of the following comments as applicable to each company:

- Please expand your discussion of the reasons you believe that your leadership structure is appropriate, addressing your specific characteristics or circumstances. In your discussion, please also address the circumstances under which you would consider having the chair and CEO roles filled by a single individual, when shareholders would be notified of any such change and whether you will seek prior input from shareholders.

Please also disclose how the experience of your lead independent director is brought to bear in connection with your board's role in risk oversight.

- Please expand upon the role that your lead independent director plays in the leadership of the board. For example, please enhance your disclosure to address whether or not your lead independent director may:
    - represent the board in communications with shareholders and other stakeholders;
    - require board consideration of, and/or override your CEO on, any risk matters; or
    - provide input on design of the board itself.
- Please expand upon how your board administers its risk oversight function. For example, please disclose:
    - why your board elected to retain direct oversight responsibility for strategic risks and other risk areas not delegated to a committee, including cybersecurity matters, rather than assign oversight to a board committee;
    - the timeframe over which you evaluate risks (e.g., short-term, intermediate-term or longterm) and how you apply different oversight standards based upon the immediacy of the risk assessed;
    - whether you consult with outside advisors and experts to anticipate future threats and trends, and how often you reassess your risk environment;
    - how the board interacts with management to address existing risks and identify significant emerging risks;
    - whether you have a chief compliance officer and to whom this position reports; and
    - how your risk oversight process aligns with your disclosure controls and procedures.

The SEC staff's issuance of these comments reflects its view that the disclosures provided in response to Item 407(h) of Regulation S-K have become increasingly standardized and are not tailored to provide meaningful information to investors.

Notably, the SEC staff issued these comments on a prospective basis, asking companies to confirm in their response letters that they will enhance their disclosures in the future. The comments do not require companies to amend their past filings, and the SEC staff noted that it is not seeking to review proposed disclosures in response to these comments.

Companies should consider proactively enhancing their board leadership structure and risk oversight disclosures in their 2023 proxy statements to provide more company-specific detail about the board's role in risk oversight and the relationship between the board's leadership structure and risk management matters. We also recommend that companies consider the 2009 adopting release for Item 407(h) of Regulation S-K for helpful guidance when preparing disclosures regarding board leadership structure and risk oversight. Companies should remain mindful that the SEC's expected new disclosure rules for climate change and cybersecurity matters will likely mandate enhanced disclosures relating to board oversight of climate-related risks and cybersecurity risks.[7]

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[7] For further background and discussion on the SEC's proposed rules on disclosures relating to board oversight of climate-related risks and cybersecurity risks, see our client alerts "SEC Proposes New Rules for Climate-Related

Consider Recommendations To Increase Board Diversity and Expertise and Enhance Related Disclosures

Board diversity is expected to continue to be, and climate and cybersecurity expertise are expected to newly be, significant focus areas for the upcoming 2023 proxy season. Companies should consider proactively taking steps to comply with applicable board diversity disclosure rules and investor requests to increase diversity in the boardroom. In addition to board diversity, boards should more broadly assess their composition and skills to determine whether the board already has or may consider adding directors with expertise in climate-related risk and cybersecurity risk. As discussed in more detail in the section of this guide titled "Note the Status of Recent and Pending SEC Rulemakings," the SEC's proposed rules regarding cybersecurity and climate-related matters are not yet final, giving companies time to consider enhancing disclosure regarding board expertise in these areas.

Sustained Focus on Board Diversity

Companies should continue to be mindful of investor expectations related to board diversity, including investor voting policies and proxy advisory firm guidelines. For example, in January 2022, State Street Global Advisors (SSGA) CEO Cyrus Taraporevala announced in his annual letter to board chairs primary stewardship priorities for 2022, including a focus on the diversity of boards and workforces. SSGA concurrently published updated guidance on enhancing gender, racial and ethnic diversity disclosures and reinforcing last year's voting policies relating to diversity disclosures. SSGA will continue to vote against the chair of the nominating and governance committee at S&P 500 and FTSE 100 companies that do not (i) disclose the racial and ethnic composition of their boards and (ii) have at least one director from an underrepresented community on the board. In 2022, SSGA implemented a voting policy expecting boards of companies in all markets and indices to have at least one female board member. Beginning in the 2023 proxy season, SSGA will expect companies in the Russell 3000, TSX, FTSE 350, STOXX 600 and ASX 300 indices to have boards comprised of at least 30% women directors. SSGA may waive the policy if a company engages with SSGA and provides a specific, timebound plan for reaching 30% representation of women directors.

Similarly, in 2021, Vanguard funds began voting against directors, including nominating committee chairs, at companies where progress on board diversity fell behind market norms and expectations.

Fidelity International highlighted in its July 2022 sustainable investing report that improving board diversity remains a priority. Fidelity generally will continue, in certain markets that include the U.S., the U.K. and the EU, to vote against reelection of directors at companies where women comprise less than 30% of the boards of directors.

As discussed in the section of this guide titled "Assess the Impact of Proxy Advisory Voting Guidelines by ISS and Glass Lewis," ISS has proposed to generally recommend against the chair of the nominating committee (or other directors on a case-by-case basis) at a company with no

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Disclosures" (March 24, 2022) and "SEC Proposes New Rules for Cybersecurity Risk Management, Strategy, Governance and Incident Disclosure" (March 11, 2022).

women on the board of directors. ISS would make an exception if there was at least one woman on the board at the preceding annual meeting and the board makes a firm commitment to return to a gender-diverse status within a year. A one-year grace period would apply to companies that have no women on their boards but have at least one director who is disclosed as identifying as nonbinary. Beginning in 2023 for Russell 3000 companies, Glass Lewis will generally recommend against the chair of the nominating committee of a board where less than 30% of the board features gender diversity. For companies outside the Russell 3000 index, Glass Lewis' existing policy requiring a minimum of one gender-diverse director will remain in place. Additionally, beginning in 2023 for Russell 1000 companies, Glass Lewis will generally recommend against the chair of the nominating committee of a board without a director from an underrepresented community.

Diversity Disclosure Trends

While the SEC's Spring 2022 rulemaking agenda anticipates new disclosure rules related to corporate board diversity, the SEC has not yet issued any proposed rules. Nonetheless, in 2022, many companies voluntarily expanded their public disclosures related to board diversity, and companies are increasingly using their proxy statements to provide investors with more clarity on how diversity, equity and inclusion matters are addressed. In 2022, approximately 93% of S&P 500 companies disclosed the racial or ethnic composition of their boards, compared to 60% in 2021.[8] Approximately 34% of Russell 3000 companies provided such disclosure in 2022, an increase compared to the prior year.[9] This reporting trend is expected to continue in the upcoming proxy season given the sustained investor focus on board diversity and the implementation of the Nasdaq rules discussed below.

Nasdaq Board Diversity Rules

In 2022, Nasdaq-listed companies became subject to two new requirements: (i) making annual public disclosure of board level diversity statistics using a standardized matrix template under Nasdaq Rule 5606 and (ii) complying with, or disclosing why they do not have, board diversity objectives under Nasdaq Rule 5605(f).

Board Diversity Matrix: Nasdaq-listed companies are required to disclose, following a standardized matrix format, the number of directors who self-identify according to specified categories, including gender, race/ethnicity and LGBTQ+ status. Many companies solicited this information, as well as individual consent to use of such information in company disclosures, from directors and nominees through the annual D&O questionnaire process.[10] Each Nasdaq-listed company should continue to include the required matrix disclosure in its proxy statement, annual report on Form 10-K or Form 20-F, as applicable, or on the company's website.[11]

Comply or Explain Requirement: Nasdaq Rule 5605(f) requires companies to meet specified board diversity objectives or otherwise explain the company's reasons for not meeting such

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[8] See the 2022 U.S. Spencer Stuart Board Index

[9] See The Conference Board/ESGAUGE Corporate Board Practices in the Russell 3000, S&P 500, and S&P MidCap 400: Live Dashboard.

[10] For additional guidance on gathering information to prepare the matrix, including sample questions, refer to Nasdaq's FAQ 1803 (August 24, 2021).

[11] For additional guidance on posting the matrix on a website, see Nasdaq's FAQ 1755 (August 6, 2021).

objectives. Subject to limited exemptions and transition periods, companies will be required to have, or explain why they do not have, one diverse director by August 7, 2023, and two diverse directors by August 6, 2025, or 2026, depending on the listing tier.[12] Companies can reference Nasdaq's related FAQs to understand and assess compliance with the new rules.

Legal Challenges to New Rules: In 2021, shortly after the SEC issued a final order approving the Nasdaq proposed rule requiring board diversity, the Alliance for Fair Board Recruitment filed a petition for review in the Fifth U.S. Circuit Court of Appeals, arguing that Nasdaq Rule 5605(f) is unconstitutional because it will compel companies to unlawfully discriminate on the basis of gender, race and sexual orientation when selecting directors. The plaintiffs claim that the SEC's approval of this rule exceeds the agency's authority under federal securities law and violated the Equal Protection Clause of the U.S. Constitution and federal anti-discrimination laws.[13] The SEC has argued that the government has no role in enforcing the rule, and therefore, the rule's constitutionality is not in question. The Fifth Circuit heard oral arguments on August 29, 2022, and the outcome of the suit remains to be seen.[14] Given the legal uncertainty surrounding Nasdaq's board diversity disclosure requirements, companies should continue to comply with Nasdaq rules and monitor legal challenges moving forward.

State Diversity Laws

Companies may be subject to additional state law-based board diversity requirements and should confirm applicability of those.[15] However, some states may be deterred from enforcing such requirements after two state courts deemed California's board diversity laws[16] unconstitutional under the state's equal protection clause.[17] The judge in each case enjoined the state from spending taxpayer money to implement or enforce the board diversity laws. However, on September 16, 2022, the appellate court in each case temporarily stayed each injunction to the extent it prevented the California secretary of state from collecting and reporting board diversity data. The temporary stays therefore enable the state to continue to collect diversity data on corporate disclosure forms pending the resolution of its appeal of the injunctions. The California secretary of state has appealed the state court decisions. Federal court proceedings challenging the same laws under the U.S. Constitution are currently on hold in the Ninth U.S. Circuit Court of Appeals until the outcome of the appeal of either state decision is determined. While legal

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[12] Nasdaq clarified deadlines for initial compliance in its FAQ 1748 (August 13, 2021).

[13] See our January 19, 2022, client alert "Rulings in 2022 Could Bring Clarity on California and Nasdaq Board Diversity Mandates."

[14] See Alliance for Fair Board Recruitment v. SEC, 5th U.S. Circuit Court of Appeals, No. 21-60626.

[15] States have passed laws similar to the exchange's rules. For example, New York law requires companies that are "authorized to do business in [the] state" to disclose the number of women on their boards. Illinois law requires any public company for which the principal executive office is located in Illinois to annually report to the secretary of state the number of board members who identify as women or racially or ethnically diverse and other information relating to board and management diversity. Washington law requires each public company incorporated in Washington state to comply with board gender thresholds or otherwise provide public disclosure of the company's approach to developing and maintaining diversity on its board.

[16] AB 979, enacted in September 2020, required companies to have at least one director from an underrepresented community by the end of 2021 and two or three such directors by the end of 2022, depending on board size. In addition, a related California law enacted in 2018, SB 826, mandated that boards with five members have at least two female members and those with six or more members have at least three female members by December 2021. Both laws required companies to report compliance to the California secretary of state, who would be authorized to impose fines of $100,000 for a first-time violation and $300,000 for each subsequent violation.

[17] See our article in the Harvard Law School Forum on Corporate Governance "Recent Ruling on Board Diversification" (May 8, 2022).

proceedings related to state board diversity laws will likely continue, companies can continue to work toward achieving their board diversity goals.

Cybersecurity Board Expertise Disclosure

On March 9, 2022, the SEC proposed new rules on cybersecurity risk management, strategy, governance and incident disclosure.[18] The proposed rules would require disclosure about the cybersecurity expertise of members of the board of directors, including the names of relevant directors and a description of the nature of their expertise. Proposed Item 407(j)(1)(ii) includes the following nonexclusive list of criteria for determining cybersecurity expertise: (i) whether the director has prior cybersecurity work experience; (ii) whether the director has obtained a certification or degree in cybersecurity; and (iii) whether the director has knowledge, skills or other background in cybersecurity. Similar to the SEC's safe harbor for "audit committee financial experts," the proposed rules note that a person who is determined to have expertise in cybersecurity will not be deemed an expert for any purpose, including, without limitation, for purposes of Section 11 of the Securities Act of 1933, as a result of being designated or identified as a director with expertise in cybersecurity pursuant to proposed Item 407(j). Companies may use the time prior to issuance of the final rule to review and assess their boards' skills and experience and to consider enhancing related disclosures on cybersecurity expertise.

Climate-Related Board Oversight and Expertise Disclosure

On March 21, 2022, the SEC proposed new rules to enhance and standardize climate-related disclosures for investors.[19] The proposed rules would require companies to provide detailed disclosures, including identifying any board members or board committees responsible for the oversight of climate-related risks. The responsible board committee may be an existing committee, such as the audit committee or risk committee, or a separate committee established to focus on climate-related risks. The proposed rules would also require disclosure of whether any director has expertise in climate-related risks, "in sufficient detail to fully describe the nature of the expertise." While certain companies have provided climate-related risk disclosures in their proxy statements and annual reports in response to an increased focus by shareholders and other stakeholders on board oversight of risk, most companies will need to take additional time to prepare disclosures that include the level of detail required by the proposed rules. Companies may use the time prior to issuance of the final rule to review and assess their boards' skills, whether their boards have established committee oversight of climate-related risks and whether any board members have expertise in climate-related risk.

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[18] See our March 11, 2022, client alert "SEC Proposes New Rules for Cybersecurity Risk Management, Strategy, Governance and Incident Disclosure."

[19] See our March 24, 2022, client alert "SEC Proposes New Rules for ClimateRelated Disclosures."

Assess the Impact of Proxy Advisory Voting Guidelines by ISS and Glass Lewis

Proxy advisory firm ISS has proposed updates to its voting guidelines,[20] and Glass Lewis has updated its voting guidelines for the 2023 annual meeting season.[21] Companies should assess the potential impact of these updates when considering changes to their corporate governance practices, shareholder engagement and proxy statement disclosures.[22] Companies should also keep in mind that ISS often includes policy updates in its final voting policy that did not appear in the proposed updates.

Climate Change: ISS' proposed guidelines include an expansion of its policy on climate board accountability. The advisory firm introduced the policy in selective markets in 2022, including the U.S. and continental Europe, and will apply it globally under the proposed guidelines. ISS will also update the factors it considers when determining whether a company is adequately disclosing climate risks, such as according to the recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD).

Glass Lewis' updated ESG policies state that companies with material exposure to climate risk due to their operations should provide thorough climate-related disclosures in line with the recommendations of the TCFD, and the boards of such companies should have explicit and clearly defined oversight responsibilities for climate-related issues. If disclosure regarding these matters is absent or significantly lacking, Glass Lewis may recommend voting against company directors. In addition, Glass Lewis' updated voting guidelines provide that it will generally recommend voting against the governance committee chair of a Russell 1000 company that does not provide explicit disclosure, such as in the company's proxy statement and governing documents, concerning the board's role in overseeing environmental and social matters.

Board Gender Diversity: ISS currently will recommend voting against the chair of the nominating committee (or other directors as appropriate), with limited exceptions, of an all-male board of directors, unless the company has included proxy statement disclosure of a "firm commitment" to appoint at least one woman to the company's board within a year. Under the proposed guidelines, beginning on February 1, 2023, the policy will expand as applicable to companies beyond the Russell 3000 and S&P 1500 indices and include foreign private issuers. In addition, the proposed guidelines include a one-year grace period for a company to come into compliance where the board includes no women but does include at least one director who is disclosed as identifying as nonbinary.

As announced in its 2022 guidelines, in 2023, Glass Lewis will generally recommend voting against nominating committee chairs of boards of Russell 3000 companies that are not at least 30% gender-diverse. Depending on the circumstances, Glass Lewis may extend its voting recommendation to additional members of the nominating committee. In determining its

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[20] See ISS' "Proposed ISS Benchmark Policy Changes for 2023" (November 4, 2022). ISS' final proxy voting guidelines for 2023 are expected to be released in early December 2022.

[21] See Glass Lewis' "2023 Policy Guidelines — United States" (November 18, 2022) and "2023 Policy Guidelines — ESG Initiatives" (November 18, 2022).

[22] For compensation-related updates regarding ISS and Glass Lewis' 2023 guidelines, see the section of this guide titled "Incorporate Lessons Learned From the 2022 Say-on-Pay Votes and Compensation Disclosures and Prepare for 2023 Pay Ratio Disclosures."

recommendation, Glass Lewis will consider company disclosure of its diversity considerations and may refrain from recommending that shareholders vote against directors if the board has provided a sufficient rationale or plan to address its lack of diversity.

Delaware Officer Exculpation Proposals:[23] In August 2022, the DGCL was amended to authorize the exculpation of officers in connection with direct claims brought by shareholders. In connection with the amendments, ISS' proposed guidelines state that ISS will generally recommend voting for proposals providing for exculpation provisions in a company's charter, including exculpation of some, but not all, officers.

Glass Lewis will evaluate proposals to adopt officer exculpation provisions on a case-by-case basis and will generally recommend voting against proposals eliminating monetary liability for breaches of the duty of care for certain corporate officers, unless the board provides a compelling rationale for eliminating the liability and the provisions are considered reasonable.

Politics and Lobbying Proposals: ISS' proposed guidelines provide that ISS generally will recommend voting on a case-by-case basis on proposals requesting greater disclosure of a company's alignment of political contributions, lobbying and electioneering spending with the company's publicly stated values and policies. In determining its recommendation, ISS will consider:

- the company's governance, oversight and disclosure related to direct political contributions, lobbying activities and payments to groups that may be used for political purposes;
- the company's disclosure regarding the reasons for its support of political candidates, trade associations or other political activities;
- incongruencies between the company's political expenditures and its publicly stated values and priorities; and
- recent significant controversies related to the company's lobbying, political contributions or political activities.

Other Matters: Additional updates to ISS' and Glass Lewis' voting guidelines are summarized below:

- ISS' proposed updates include a recommendation that shareholders vote against relevant directors at all U.S. companies with unequal voting rights.
- ISS' proposed updates also end the current one-year transition period delaying adverse vote recommendations against companies with capital structures that provide for unequal voting rights.
- For certain U.S. domestic issuers incorporated outside the U.S. and listed solely on a U.S. exchange, ISS would generally recommend voting for resolutions to authorize the issuance of common shares representing up to 20% of a company's currently issued common share capital if the issuance is not tied to a specific transaction or financing proposal.

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[23] For related updates, see the section of this guide titled "Consider New DGCL Amendments Permitting Officer Exculpation."

- Glass Lewis will generally recommend against the chair of the nominating committee of a board of a Russell 1000 company (a) with fewer than one director from an underrepresented community or (b) that has not provided any disclosure regarding certain director diversity and skills matters.
- Glass Lewis revised its "overboarding" policy and will generally recommend against a director who serves as an executive officer (other than executive chair) of a public company while serving on more than one external public company board, a director who serves as an executive chair of any public company while serving on more than two external public company boards and any other director who serves on more than five public company boards.
- Glass Lewis may recommend against a company's nominating committee chair when the company's proxy statement does not identify the proponent or lead proponent of a shareholder proposal, and Glass Lewis' updated ESG guidelines encourage companies to provide information regarding proponents' share ownership levels and the companies' engagement with the proponents.
- Glass Lewis may recommend against relevant directors if a company experiences cyberattacks that cause significant harm to shareholders and the company has not provided clear disclosure concerning the role of the board in overseeing cybersecurity matters and how the company ensures that its directors are knowledgeable about such matters.

Note the Current Status of SEC Rules Governing Proxy Advisors

In July 2020, the SEC adopted amendments to its proxy rules that codified the SEC's position that voting advice issued by proxy advisors, such as ISS and Glass Lewis, generally constitutes a solicitation under the federal proxy rules and required certain conditions for proxy advisors to qualify for exemptions from the information and filing requirements under the proxy rules.[24]

Nearly two years later, in July 2022, the SEC, by a 3-2 vote, adopted amendments rescinding two components of the proxy rules adopted in 2020.[25] Specifically, the amendments rescinded certain conditions that proxy advisors would have to satisfy for their voting recommendations to be exempt from proxy information and filing requirements — namely (i) making the proxy advisor's voting advice available to the subject company at or before the time such advice is disseminated to the proxy advisor's clients and (ii) providing a mechanism by which the proxy advisor's clients can reasonably be expected to become aware of the subject company's written responses to such voting advice.

From a practical perspective, the amendments preserve the status quo and companies may not experience any changes in their interactions with proxy advisors as a result of these amendments, but should nevertheless be aware of the change.[26]

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[24] See our July 27, 2020, client alert "SEC Adopts Proxy Rule Amendments Relating to Proxy Voting Advice Businesses."

[25] See our July 14, 2022, client alert "SEC Rescinds Certain 2020 Amendments to Rules Governing Proxy Advisors."

[26] The conditions for proxy voting advice to qualify for an exemption from the proxy solicitation rules did not become effective until December 1, 2021. However, on June 1, 2021, the Division of Corporation Finance of the SEC

Consider Shareholder Proposal Trends and Developments

The 2022 proxy season held a number of surprises for public companies dealing with shareholder proposals. Below is a brief summary of observations and an overview of recent developments relating to Exchange Act Rule 14a-8.

2022 Proxy Season Summary

An Influx of Prescriptive Proposals, but Less Investor Interest

The number of shareholder proposals submitted to companies in the 2022 proxy season increased from the prior season — 958 in 2022, an increase from the 892 in 2021. The overall number of proposals that went to a vote also increased, from 429 in 2021 to 551 proposals in 2022.

Despite the increased number of proposals submitted and voted on, overall support for shareholder proposals weakened. The SEC also took a more restrictive posture toward no-action requests to exclude shareholder proposals, which may have led to an increase in topics on ballots in which shareholders at large were not interested. In this regard, the staff only granted no-action relief in 41% of cases in 2022, compared to 70% in the prior year.

Highlights of Specific Proposal Topics

Environmental and Social (E&S) Proposals: For the sixth year in a row, E&S proposals outpaced the total number of governance proposals submitted to companies, with 573 E&S proposals submitted compared to 332 governance-focused proposals. Consequently, more E&S proposals (279) than governance proposals (236) ultimately landed on companies' ballots. Thirty-six E&S proposals received majority support in 2022, about the same number as in 2021 (37).

Notably, a large number of environmental proposals (226) were submitted to companies, which addressed a broad range of topics. In contrast to 2021, a relatively large number (90) of environmental proposals ultimately moved to a vote in 2022. Average support for those proposals that appeared on ballots, however, was approximately 31%, less than the approximately 37% average support level seen in 2021.

Shareholders submitted to companies roughly the same number of proposals addressing social issues in 2022 as shareholders did in 2021, with 347 social proposals submitted in the 2022 proxy season (compared to 346 in 2021). More of these proposals moved forward onto companies' ballots in 2022 (189) as compared to 2021 (111). Average support for these social proposals decreased to 26% in 2022 as compared to the 36% average support level seen in 2021. Twenty-one social proposals received majority support in 2022, about the same amount as in 2021 (23).

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issued guidance that it would not recommend enforcement action to the SEC based on the 2020 amendments while the SEC considered whether to take further regulatory action regarding the 2020 amendments.

Continuing a trend seen in 2021, proposals relating to diversity, equity and inclusion (DEI) continued to grow in number. One type of DEI proposal that related to civil rights and racial equity audits received 41 shareholder proposals in 2022 (of which 24 moved forward to a vote) with 44% average support (as compared to 14 proposals in 2021 of which 10 moved forward to a vote with 34% support). Eight of these proposals received majority support in 2022 (while none of this proposal type received majority support in 2021).

Governance Proposals: As compared to the 2021 season, a smaller percentage of the proposals that moved forward to a vote in 2022 concerned governance-related topics, with 236 out of 567 proposals addressing governance topics in 2022 (compared with 249 out of 429 in 2021). Forty governance proposals received majority support in 2022, a decrease from 52 in 2021.

The most popular governance topic in 2022 related to requests to provide for, or make easier, the ability of shareholders to call a special meeting, with 119 proposals submitted, 111 voted on (with 37% average support) and 10 receiving majority support, all up from 37 special meeting proposals submitted in 2021, 31 voted on (with 34% average support) and four receiving majority support.

Proposals calling for an independent chair were the second most common governance topic in 2022, with 39 proposals voted on (compared to 35 in 2021). Average support for independent chair proposals decreased slightly to approximately 29% in 2022 from approximately 31% in 2021, with none of these proposals receiving majority support in 2022 (compared to one that received support in 2021). Generally these proposals fail to achieve majority support absent a larger governance issue at the company.

The third most common governance topic in 2022 related to requests to adopt or amend proxy access rights. The number of proxy access proposals voted on in 2022 decreased to 13 from 29 in 2021, and the average support declined to approximately 32% in 2022 from 34% in 2021.

Executive Compensation Proposals: The number of executive compensation-related proposals submitted in 2022 increased to 53 from 52 in the 2021 proxy season. The number of executive compensation-related proposals that moved forward to a vote also increased — to 36 in 2022 from 25 in 2021 — and the proposals voted on in 2022 had higher average support of approximately 34% (compared with approximately 20% in 2021).

The increase in the number of compensation proposals that moved forward to a vote in 2022 and the higher average support was largely the result of 17 proposals voted on that related to shareholder approval of severance arrangements (with 45% average support).

Four executive compensation proposals received majority support in 2022 (after only one received majority support in 2021). All four proposals that received majority support in 2022 related to shareholder approval of severance arrangements.

Effect of Staff Legal Bulletin No. 14L

In November 2021, the SEC staff issued Staff Legal Bulletin No. 14L (SLB 14L), which had a significant effect on the no-action letter process during the 2022 proxy season. In SLB 14L, the

staff took the unprecedented action of rescinding staff guidance published under the previous SEC administration. This ultimately led to the reversal of a number of no-action decisions published in prior years.

While SLB 14L indicated that the staff would revert to using a historical approach to no-action letters, results seemed to indicate that a new approach was in effect. As noted above, the number of no-action letters granted declined dramatically. A number of long-standing staff positions, even those predating the rescinded Staff Legal Bulletins, also were reversed. For example:

Ordinary Business Matters

- **Litigation Strategy:** Historically, the SEC staff has shown deference to arguments that a proposal might affect litigation to which a company is a party, even where a significant policy issue is implicated. Some staff decisions in the 2022 proxy season appeared to deviate from this approach, however, as the staff denied no-action relief for a proposal relating to a third-party civil rights audit where the company argued that the proposal would interfere with its litigation strategy. In the 2021 proxy season, the staff granted relief for a similar proposal where the company was involved in relevant litigation.
- **Human Capital Management:** SLB 14L noted that proposals "squarely raising human capital management issues with a broad societal impact would not be subject to exclusion solely because the proponent did not demonstrate that the human capital management issue was significant to the company." This approach was evident, but often at odds with historical precedent, in the 2022 proxy season. In one case, the staff denied no-action relief for a proposal that asked the company to adopt and disclose a policy requiring that all employees accrue paid sick leave. The staff had permitted exclusion of a similar proposal in the 2021 proxy season.
- **Micromanagement:** SLB 14L outlined a revised and more stringent approach to the micromanagement prong of the ordinary business exclusion. Specifically, the staff explained that its previous approach (under the rescinded Staff Legal Bulletins) may have "been taken to mean that any limit on company or board discretion constitutes micromanagement." The staff stated in SLB 14L that it will take a "measured approach" to micromanagement arguments, focusing on "the level of granularity sought in the proposal and whether and to what extent it inappropriately limits discretion of the board or management." SLB 14L noted that the staff will not concur with the exclusion of proposals addressing climate change that "suggest targets or timelines so long as the proposals afford discretion to management as to how to achieve such goals."

Substantial Implementation

- **Eliminating Supermajority:** The staff appeared to apply new standards to substantial implementation arguments relating to proposals seeking to eliminate supermajority voting requirements in companies' governing documents. In one example, the staff rejected an argument that a company substantially implemented a proposal requesting it replace greater-than-simple-majority voting requirements in its charter and bylaws with a majority-of-votes-cast standard where the company explained that its governing documents did not contain any supermajority voting provisions. The denial was based on the fact that the company appeared to be subject to certain supermajority voting requirements under

applicable state law and that the company's governing documents did not otherwise provide for a lower voting standard.

- **Proxy Access:** In precedent going back to 2016, the staff agreed that adopting a typical "3-3-20-20" proxy access bylaw substantially implemented proposals requesting adoption of proxy access rights for an unlimited number of shareholders holding at least 3% of a company's shares for at least three years. In a number of instances in the 2022 proxy season, however, the staff denied no-action requests, seemingly because the bylaw did not provide for an unlimited number of shareholders to aggregate their holdings

In summary, SLB 14L seemed to open the floodgates for shareholder proponents and as a result, shareholders were presented with more proposals on a wider range of topics with which they often disagreed.

Proposed Amendments to Rule 14a-8

On July 13, 2022, the SEC proposed amendments that would modify the standards for exclusion under the "substantial implementation," "duplication" and "resubmission" bases for exclusion of Rule 14a-8. Although presented as an effort to provide greater certainty and transparency to shareholder proponents and companies, the amendments (if adopted as proposed) likely would increase the number of shareholder proposals received by companies and make it less likely that proposals could be excluded.

Substantial Implementation: Rule 14a-8(i)(10) allows a company to exclude from the company's proxy materials a shareholder proposal that "the company has already substantially implemented." In determining whether a proposal has been substantially implemented, the staff assesses whether a company's particular policies, practices and procedures "compare favorably" with the guidelines of the proposal, whether the company has addressed the proposal's underlying concerns and whether the essential objectives of the proposal have been met. Historically, a proposal could be excluded on the basis of substantial implementation even if a company had not implemented all of the proposal's requested elements.

The proposed amendments would provide that a company may exclude a proposal as substantially implemented "[i]f the company has already implemented the essential elements of the proposal." In particular, the proposing release notes that the proposed amendment would permit a shareholder proposal to be excluded as substantially implemented only if the company has implemented all of the shareholder proposal's essential elements.

Duplication: Rule 14a-8(i)(11) provides that a company may exclude a shareholder proposal from the company's proxy materials if the proposal "substantially duplicates [by sharing the same "principal thrust" or "principal focus"] another proposal previously submitted to the company by another proponent that will be included in the company's proxy materials for the same meeting." The proposed amendments would specify that a proposal "substantially duplicates" another proposal previously submitted for the same shareholder meeting if it "addresses the same subject matter and seeks the same objective by the same means."

Resubmission: Rule 14a-8(i)(12) provides that a company may exclude a shareholder proposal from the company's proxy materials if the proposal "addresses substantially the same subject matter" as a proposal that was included in the company's proxy materials, voted on in the last

three years and failed to received support above a certain threshold. The proposed amendments would provide that a proposal qualifies as a resubmission only if it “substantially duplicates” a previous proposal that failed to receive support above a certain threshold, meaning that it “addresses the same subject matter and seeks the same objective by the same means.”