PART I: MOST COMMON REASONS FOR A LOW SAY ON PAY VOTE (2023)

HUGESSEN CONSULTING

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In this briefing, we delve into the most common reasons why shareholders vote against a company's advisory vote on executive compensation (Say on Pay). We also highlight the reasons why proxy advisory firms (Institutional Shareholder Services (ISS) and Glass Lewis) commonly recommend voting against Say on Pay. In Part II, Hugessen will conduct an analysis assessing the impact that a negative recommendation from one or both proxy advisors might have on a company's Say on Pay vote.

Methodology

We reviewed the rationales provided by institutions shareholders of S&P/TSX issuers that received a Say on Pay score of below 80% in 2023 (n=30)[1]. We also gathered compensation-related flags raised by ISS and Glass Lewis when determining their Say on Pay vote recommendations for this same group of companies.

Key Findings

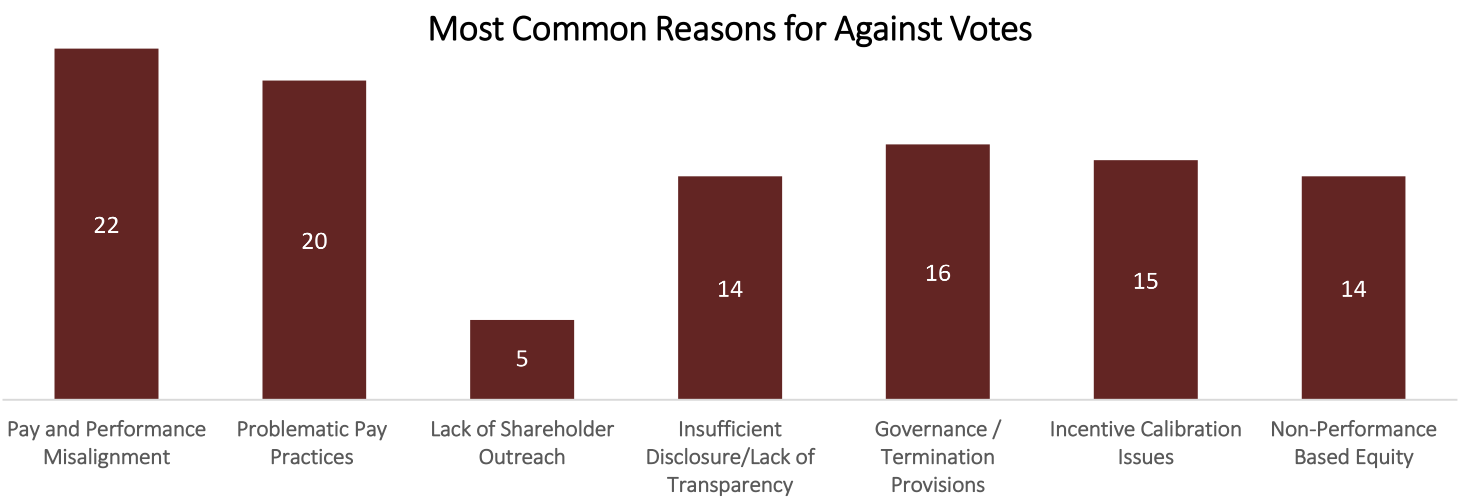
The most common reasons behind 'against' votes on Say on Pay in 2023 were **pay and performance misalignment and problematic pay practices**. This was consistent with the most common rationales proxy advisors identified when recommending against these votes (see next page) .

While many sophisticated institutional investors conduct their own proxy voting analysis, the proxy advisors still play an influential role opining on Say on Pay. Among this group of 30 companies with sub-80% Say on Pay results, 26 received an against vote recommendation from either from ISS or Glass Lewis, with 7 receiving an against vote recommendation from both.

Why Shareholders Voted Against Say on Pay

Summarized below are the most commonly disclosed reasons why shareholders voted against Say on Pay for the 30 companies in our study. We note that it is common for companies to receive rationales flagging more than one issue (e.g. a pay for performance misalignment and an incentive calibration issue).

Note: This does not represent an exhaustive list; shareholders are not required to disclose the rationale behind their vote, thus this captures only voluntary disclosure.

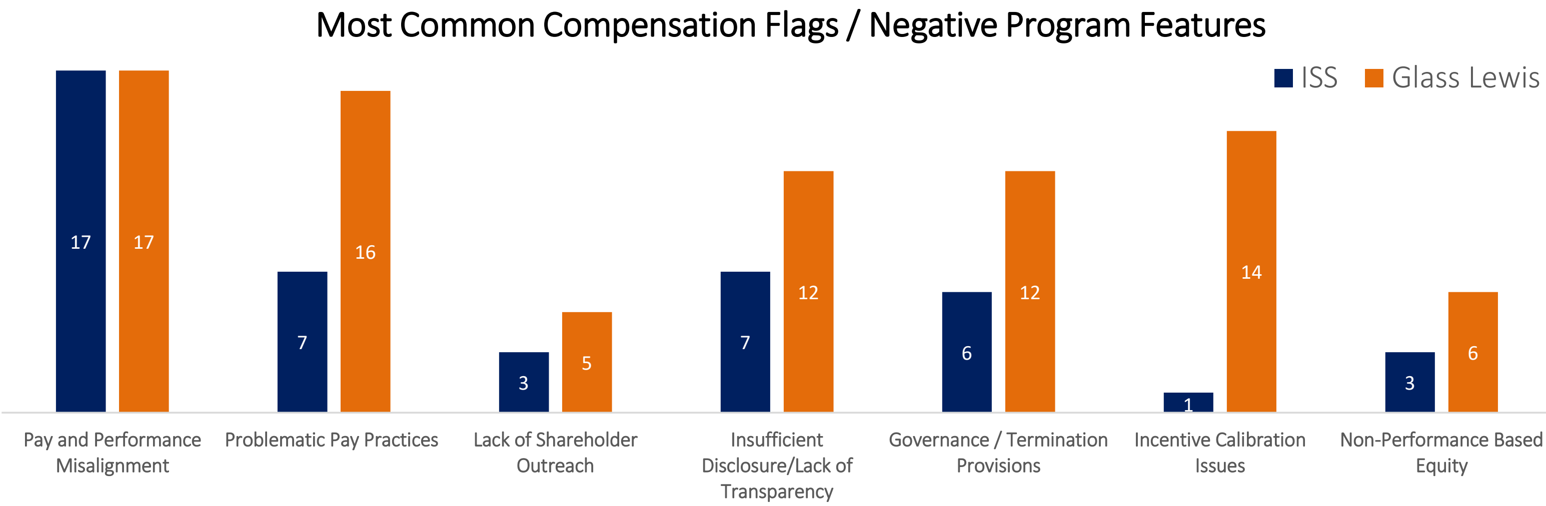


Note: Companies may be categorized under multiple buckets.
Problematic pay practices examples include one-time awards, quantum-related concerns, CEO pay ratio disparity, among others.

[1]Data summarized from Diligent's Market Intelligence Voting Module

Flags from ISS and Glass Lewis

Summarized below are the most common compensation flags / negative program features outlined by ISS and Glass Lewis among the 30 companies in our study. Glass Lewis was more likely to identify issues with program structure and design than ISS was.



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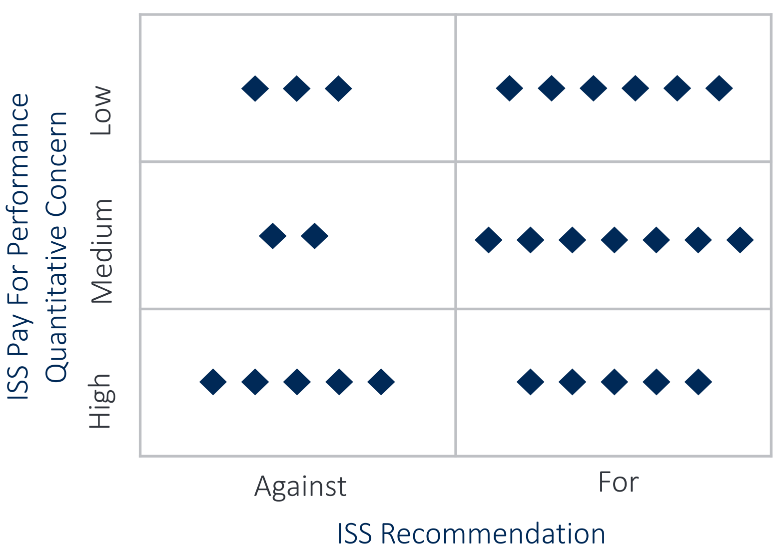
Problematic pay practices examples include one-time awards, quantum-related concerns, CEO pay ratio disparity, among others.

ISS Pay for Performance Concern and Corresponding Say on Pay Recommendation

In the exhibit below, we showcase the relationship between ISS' quantitative Pay for Performance concern grade and their corresponding vote recommendation on Say on Pay from the dataset. Note: Only 28 of the 30 companies in our study had a pay for performance evaluation conducted by ISS.



A high pay for performance concern level does not equate to an automatic against recommendation by ISS on Say on Pay for a company. ISS reviews these on a case-to-case basis to determine their final recommendation.

Select supporting rationales provided by ISS to recommend a vote for a company's Say on Pay, despite having a high pay for performance concern, include:

- Strong relative performance on non-TSR financial metrics (ISS Financial Performance Assessment)
- Strong pay for performance alignment relative to a company's self-selected peer group
- Significant weighting on performance-based compensation
- Overall reduction/forfeiture of CEO pay

Conclusion

As we enter the 2024 proxy season, understanding the most common reasons why proxy advisors recommend, and shareholders vote against Say on Pay can help issuers prepare for and respond to potential issues. Having an awareness of shareholder views ahead of the annual general meeting (AGM) will limit any surprises.

Hugessen supports clients throughout the year in making the right decisions on executive compensation in an environment of heightened complexity and scrutiny. This may include identifying issues ahead of the AGM (Hugessen is able to conduct in-house pay for performance simulations using disclosed ISS and Glass Lewis quantitative methodologies) and/or providing advice on how best to address them (incentive program design changes, proxy circular disclosure, shareholder engagement, etc.).