



Proposed ISS Benchmark Policy Changes for 2024

Request for Comments

Comment Period: November 21, 2023, through November 30, 2023

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Introduction

ISS Governance is announcing the opening of our benchmark voting policy comment period on proposed changes for 2024. The comment period will be open from November 21, through 5:00 p.m. ET on November 30, 2023. This year there are fewer proposed changes than in the last few years. We invite views and comments from all interested parties on policy changes¹. This year, there are four (4) proposed voting policy changes for 2024; they are related to Canada, Japan, and the Asia-Pacific policy guidelines.

To ensure ISS benchmark voting policy changes take into consideration a broad range of perspectives, including the views of institutional investors globally and those of the broader corporate governance community, ISS gathers input each year from institutional investors, companies, and other market constituents through a variety of channels and media. The comment period follows the recent release of the results of our [2023 Global Benchmark Policy Survey](#). Some of the questions asked in the 2023 Survey related to topics which may be used to guide policy application, potential further development of the ISS Global Voting Principles, and for consideration of policy changes beyond 2024.

Comments received will be considered as we finalize the changes for 2024. We expect to announce the final benchmark policy changes in or around mid-December 2023. The revised policies will be applied for shareholder meetings taking place on or after Feb 1, 2024, except where otherwise noted for later implementation.

To submit comments, please send via email to policy@issgovernance.com. Please indicate your name and organization in your submission.

All comments received may be published on our website, unless otherwise requested in the body of the email submission.

Key Proposed Policy Changes- Summary

Board Diversity – Canadian Policy

In 2022, a new board diversity policy was approved for Canadian S&P/TSX Composite Index constituents with a one-year grace period (to be effective as of February 1st, 2024). As we approach the end of the previously announced grace period, the transition language will now be removed, and the final policy framework is being included in the comment period document to provide transparency on the policy framework.

Since 2020, Canada has broadened disclosure requirements on board diversity for publicly traded corporations beyond gender, mandating businesses to report on four employment equity groups (women, visible minorities, Indigenous peoples, and persons with disabilities) through new requirements introduced to the Canada Business Corporations Act (CBCA) in Bill C-25. According to the Government of Canada, these measures aim to foster diversity at the highest levels of corporate leadership in Canada, improve shareholder democracy, and help investors make better and more informed decisions through better transparency.

¹ ISS will be making some additional changes to policy that it does not consider something on which we should solicit comments, such as to make its policy adhere to local governance laws or codes and to take out transitional language.

Distributing corporations established under the CBCA are required to disclose both to their shareholders (through their proxy circulars), and to Corporations Canada, information regarding the diversity of their boards and senior management. The disclosure must include the representation of various designated groups on the board and among senior management. These designated groups include women, Indigenous peoples (First Nations, Inuit and Métis), persons with disabilities and members of visible minorities. In addition, the CBCA requires distributing corporations to disclose whether they have a diversity and inclusion policy, and if not, to provide an explanation why not. This "comply or explain" approach is not prescriptive but is intended to foster a dialogue between distributing corporations and their shareholders, increase corporate transparency and support the push for increased diversity on boards and in senior management. The full implementation of this benchmark policy, following the end of the previously announced grace period, will align the ISS policy for Canadian S&P/TSX Composite Index more closely with the ISS US policy guidelines for Russell 3000 and/or S&P 1500 indices on racial/ethnic diversity.

Election of Directors – Japan Policy

This proposed policy change will reinstate the application of the “return on equity” (or ROE) policy for Japanese companies under ISS benchmark policy. Until 2020, ISS’ Japan benchmark policy generally recommended votes against the re-election of the top executives at companies that underperformed in terms of capital efficiency (i.e., when the company had posted average ROE of less than 5 percent over the previous five fiscal years), unless an improvement (defined as ROE of 5 percent or greater for the most recent fiscal year) was observed. However, it was decided that the impact of the COVID-19 pandemic on companies’ operating performance reduced the appropriateness of using ROE to measure capital efficiency during the emergency. The application of the ROE policy has been suspended since June 2020.

However, now that the pandemic has receded, the temporary suspension is no longer relevant. Overall, Japanese companies’ operating performance has generally improved, and the median ROE of Japanese companies with fiscal years ending March 2023 improved to 6.8 percent. In response to the ISS 2023 Policy Survey, out of 184 investor respondents to the question “Do you think it is appropriate for ISS to resume the application of the ROE policy for Japanese companies?” 77 percent of respondents answered “yes.” Out of 86 corporate respondents to the question, 60 percent answered “yes.”






Takeover Defense Plans (Poison Pills) – Japan Policy

In Japan, there has been a reduction in the number of companies with poison pills. Nonetheless, in recent years, with an increase in shareholder activism in Japan, some companies have implemented newly introduced poison pills, often designed to work against specific shareholders. Meanwhile, overall board independence of Japanese companies has improved. Based on ISS data as of June 2023, 84.3 percent of Japanese boards were comprised of at least one-third outside directors, meeting the board independence criteria in the current ISS Japan benchmark policy regarding poison pills. However, only 8.8 percent of companies covered by ISS from January to June 2023 had a majority-independent board, based on ISS criteria. The proposed poison pill policy update reflects the improving board independence in the market and signals that board independence is critical if a company seeks to deploy a poison pill. It is intended to prevent a non-independent board from arbitrarily using a poison pill mechanism for management entrenchment, particularly when pills are designed for specific shareholders.

Equity Compensation Plans – Asia-Pacific Regional markets

The Asia Pacific Regional policy is being updated to clarify and codify the policy approach regarding equity compensation plans for companies in Indonesia, Malaysia, Pakistan, Sri Lanka, Thailand, and Vietnam under the ISS Asia-Pacific Regional Policy. The proposed update outlines ISS' approach already being applied for the evaluation of stock option plans and restricted share plans for those markets and provides greater transparency of the existing framework applied on the analysis of such proposals.

ISS welcomes any comments about the four proposed policy changes, specifically on the following questions:

-  **Question:** Do you have any concerns with the proposed policy update?
-  **Question:** If the proposed change contemplates ISS adverse vote recommendations, are they implemented appropriately?
-  **Question:** If the proposed change contemplates ISS adverse vote recommendations, are the appropriate mitigating factors being considered?
-  **Question:** If the proposed change applies to a particular set of companies, is the proposed coverage universe appropriate?
-  **Question:** Are there any other factors that ISS should consider when contemplating the proposed policy update?

Policies for Comment

Board of Directors

Election of Directors – Board Diversity

1. Canada S&P/TSX – Board Racial and/or Ethnic Diversity

Current ISS Policy:	New ISS Policy:
<p>General Recommendation: For meetings on or after Feb. 1, 2024, for companies in the S&P/TSX Composite Index, generally vote against or withhold from the Chair of the Nominating Committee or Chair of the committee designated with the responsibility of a nominating committee, or the Chair of the board of directors if no nominating committee has been identified or no chair of such committee has been identified, where the board has no apparent racially or ethnically diverse members¹. An exception will be made if there was racial and/or ethnic diversity on the board at the preceding annual meeting and the board makes a firm public commitment to appoint at least one racial and/or ethnic diverse member at or prior to the next AGM.</p> <p>Evaluate on a case-by-case basis whether against/withhold recommendations are warranted for additional directors at companies that fail to meet the policy over two years or more.</p>	<p>General Recommendation: For companies in the S&P/TSX Composite Index, generally vote against or withhold from the Chair of the Nominating Committee or Chair of the committee designated with the responsibility of a nominating committee, or the Chair of the board of directors if no nominating committee has been identified or no chair of such committee has been identified, where:</p> <ul style="list-style-type: none"> ▪ The board has no apparent racially or ethnically diverse members¹. and ▪ The company has not provided a formal, publicly-disclosed written commitment to add at least one racially or ethnically diverse director at or prior to the next AGM. <p>Evaluate on a case-by-case basis whether against/withhold recommendations are warranted for additional directors at companies that fail to meet the policy over two years or more.</p>
<p>Footnotes:</p> <p>¹Aggregate diversity statistics provided by the board will only be considered if specific to racial and/or ethnic diversity.</p> <p>Racial and/or Ethnic Diversity is defined as: Aboriginal peoples (means persons who are Indigenous, Inuit or Métis) and members of visible minorities (means persons, other than Aboriginal peoples, who are non-Caucasian in race or non-white in colour). Employment Equity Act (S.C. 1995, c. 44) https://laws-lois.justice.gc.ca/eng/acts/E-5.401/section-3.html</p>	<p>Footnotes:</p> <p>¹Aggregate diversity statistics provided by the board will only be considered if specific to racial and/or ethnic diversity.</p> <p>Racial and/or Ethnic Diversity is defined by the Government of Canada as: Aboriginal peoples (means persons who are Indigenous, Inuit or Métis) and members of visible minorities (means persons, other than Aboriginal peoples, who are non-Caucasian in race or non-white in colour). Employment Equity Act (S.C. 1995, c. 44) https://laws-lois.justice.gc.ca/eng/acts/E-5.401/section-3.html</p>

Rationale for Change:

The introduction of this policy was announced in 2022, with a grace period of one year to February 2024. This year's proposed change removes the transition language and also introduces mitigation based on a publicly disclosed commitment to add at least one racially or ethnically diverse members at or prior to the next AGM.

The background to the policy is that in 2020, Canada broadened disclosure requirements on board diversity for publicly traded corporations beyond gender, mandating businesses to report on four employment equity groups (i.e., women, visible minorities, Indigenous peoples and persons with disabilities) through new requirements introduced to the Canada Business Corporations Act (CBCA) in Bill C-25. According to the Government of Canada, these measures aim to foster diversity at the highest levels of corporate leadership in Canada, improve shareholder democracy, and help investors make better and more informed decisions through better transparency.

Distributing corporations established under the CBCA are required to disclose to both their shareholders (through their proxy circulars) and to Corporations Canada information regarding the diversity of their boards and senior management. The disclosure must include the representation of various designated groups on the board and among senior management. These designated groups include women, Indigenous peoples (First Nations, Inuit and Métis), persons with disabilities and members of visible minorities. In addition, the CBCA requires distributing corporations to disclose whether they have a diversity and inclusion policy, and if not, to provide an explanation why not. This "comply or explain" approach is not prescriptive but is intended to foster a dialogue between distributing corporations and their shareholders, increase corporate transparency and support the push for increased diversity on boards and in senior management.

Based on the proxy circulars filed in 2020, the Government of Canada identified 669 distributing corporations which were required to disclose diversity information. Of these distributing corporations, the proxy circulars of 469 companies were reviewed and 85.9 percent contained information on diversity, and also concluded that there continues to be ongoing challenges in getting a complete picture of diversity because the CBCA and related regulations do not specify how distributing corporations should disclose this information. To better support corporations, in early 2021, Canadian guidelines were published to help and encourage distributing corporations to disclose their diversity information annually in a more consistent manner, and the consistency in disclosure will ensure that diversity information can be collected and analyzed in a consistent way and enable a sound year-over-year analysis that will foster steady progress toward more diverse corporate leadership. As a result of the diversity disclosure requirements and industry awareness-raising activities, distributing corporations were more aware of their filing requirements in 2021 than they were in 2020. In 2021, an average of 13 percent of the required diversity information disclosed by distributing corporations was incomplete, missing or not provided in a standardized way.

During the 2021 Canadian roundtable discussions, the vast majority of our clients had the shared view that boards should aim to reflect the company's customer base and the broader societies in which they operate by including directors drawn from racial and ethnic minority groups, and also widely supported the expectation for disclosure from companies on racial/ethnic diversity at the board level, and that all companies should disclose this information to the fullest extent possible. In addition to the information referenced above, the implementation of this benchmark policy will align the ISS Canadian S&P/TSX Composite Index policy more closely to the ISS U.S. Policy for Russell 3000 and/or S&P 1500 indices' on racial/ethnic diversity,

<https://www.ic.gc.ca/eic/site/cd-dgc.nsf/eng/cs08317.html>

<https://www.bennettjones.com/Blogs-Section/Government-of-Canada-Publishes-First-Report-on-Diversity-Disclosure>

<https://www.ic.gc.ca/eic/site/cd-dgc.nsf/eng/cs09445.html>

Election of Directors – General Recommendation

2. Japan – ROE Policy Resumption

Current ISS Policy:	New ISS Policy:
<p>General Recommendation:</p> <p>N/a*</p>	<p>General Recommendation:</p> <p>ISS has three policies for director elections in Japan: one for companies with a statutory auditor board structure, one for companies with a U.S.-type three committee structure, and one for companies with a board with audit committee structure. Among various guidelines is ROE policy, which is applied to Japanese companies regardless of board structure. Under the ROE policy: vote for the election of directors, except:</p> <ul style="list-style-type: none"> ▪ Top executive(s)¹ at a company that has underperformed in terms of capital efficiency (i.e., when the company has posted average return on equity (ROE) of less than five percent over the last five fiscal years)², unless an improvement³ is observed;
<p>Footnotes:</p> <p>*Currently, the application of the ROE policy has been suspended since 2020, as set forth in “Japan Proxy Season 2020 – Impacts of the Covid-19 Pandemic, Additional ISS Policy Guidance.”</p>	<p>Footnotes:</p> <p>¹ In most cases, the top executive will be the “shacho” (president). However, there are companies where the decision-making authority also rests with the “kaicho” (chairman of the company) or “daihyo torishimariyaku” (representative director).</p> <p>² Exceptions may be considered for cases such as where the top executive has newly joined the company in connection with a bailout or restructuring. This policy will not be applied to companies which have been public for less than five years.</p> <p>³ Improvement is defined as ROE of five percent or greater for the most recent fiscal year.</p>

Rationale for Change:

This proposed policy change will reinstate the application of the “return on equity” (or ROE) policy for Japanese companies under ISS benchmark policy. Until 2020, ISS Japan benchmark policy generally recommended votes against the re-election of the top executives at companies that underperformed in terms of capital efficiency (i.e., when the company had posted average return on equity (ROE) of less than 5 percent over the previous five fiscal years), unless an improvement (defined as ROE of 5 percent or greater for the most recent fiscal year) was observed. However, it was decided that the impact of the COVID-19 pandemic on companies’ operating performance reduced the appropriateness of using ROE to measure capital efficiency, and the application of the ROE policy has been suspended since June 2020. The suspension was stipulated in “Japan Proxy Season 2020 – Impacts of the Covid-19 Pandemic, Additional ISS Policy Guidance.”

However, now that the pandemic has receded, the temporary suspension is no longer relevant. Overall, Japanese companies’ operating performance has generally improved, and the median ROE of Japanese companies with fiscal years ending March 2023 improved to 6.8 percent. In response to the ISS 2023 Policy Survey, out of 184 investor respondents to the question “Do you think it is appropriate for ISS to resume the application of the ROE policy for Japanese companies?” 77 percent of respondents answered “yes.” Out of 86 corporate respondents to the question, 60 percent answered “yes.”

Takeover Defense Plans

3. Japan – Poison Pills

Current ISS Policy:	New ISS Policy:
<p>General Recommendation:</p> <p>Generally, vote against the approval of takeover defense plans (poison pills), unless:</p> <p>(Necessary conditions)</p> <ul style="list-style-type: none"> ▪ Independent directors who meet ISS guidelines on attendance comprise at least 1/3 of the board after the shareholder meeting; ▪ The number of independent directors who meet ISS guidelines on attendance is at least two after the shareholder meeting; ▪ The directors are subject to annual elections; ▪ The bid evaluation committee is composed entirely of independent directors, or independent statutory auditors, who meet ISS guidelines on attendance; ▪ The trigger threshold is set at no less than 20 percent of shares outstanding; ▪ The duration of the poison pill does not exceed three years; ▪ There are no other protective or entrenchment tools that can serve as takeover defenses, including blocking stakes held by management-friendly shareholders, or setting the maximum board size to the actual board size to eliminate vacant seats, or tightening of procedures for removing a director from office; ▪ The company posts its proxy circular on the stock exchange website at least four weeks prior to the meeting, to give shareholders sufficient time to study the details of the proposal and question management about them; and ▪ The pill’s total duration*does not exceed three years. <p>(Second stage of analysis, to be applied only when all necessary conditions are met)</p> <ul style="list-style-type: none"> ▪ The company has disclosed in its proxy circular specific, credible steps it is taking to address the vulnerability to a takeover by enhancing shareholder 	<p>General Recommendation:</p> <p>Generally, vote against the approval of takeover defense plans (poison pills), unless:</p> <p>(Necessary conditions)</p> <ul style="list-style-type: none"> ▪ Independent directors who meet ISS guidelines on attendance comprise a majority of the board after the shareholder meeting; ▪ The number of independent directors who meet ISS guidelines on attendance is at least two after the shareholder meeting; ▪ The directors are subject to annual elections; ▪ The bid evaluation committee is composed entirely of independent directors, or independent statutory auditors, who meet ISS guidelines on attendance; ▪ The trigger threshold is set at no less than 20 percent of shares outstanding; ▪ The duration of the poison pill does not exceed three years; ▪ There are no other protective or entrenchment tools that can serve as takeover defenses, including blocking stakes held by management-friendly shareholders, or setting the maximum board size to the actual board size to eliminate vacant seats, or tightening of procedures for removing a director from office; ▪ The company posts its proxy circular on the stock exchange website at least four weeks prior to the meeting, to give shareholders sufficient time to study the details of the proposal and question management about them; and ▪ The pill’s total duration*does not exceed three years. <p>(Second stage of analysis, to be applied only when all necessary conditions are met)</p> <ul style="list-style-type: none"> ▪ The company has disclosed in its proxy circular specific, credible steps it is taking to address the vulnerability to a takeover by enhancing shareholder



<p>value, and explained how the temporary protection afforded by the pill will help accomplish this goal.</p> <p>* The pill's total duration is defined as the sum of the number of years the company has had a pill in place and the number of years the proposed pill will be effective.</p>	<p>value, and explained how the temporary protection afforded by the pill will help accomplish this goal.</p> <p>* The pill's total duration is defined as the sum of the number of years the company has had a pill in place and the number of years the proposed pill will be effective.</p>
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Rationale for Change:

In Japan, there has been a reduction in the number of companies with poison pills. Nonetheless, in recent years, with an increase in shareholder activism in Japan, some companies have implemented newly introduced poison pills, often designed to work against specific shareholders. Meanwhile, overall board independence of Japanese companies has improved. Based on ISS data as of June 2023, 84.3 percent of Japanese boards were comprised of at least one-third outside directors, meeting the board independence criteria in the current ISS Japan benchmark policy regarding poison pills. However, only 8.8 percent of companies covered by ISS from January to June 2023 had a majority-independent board, based on ISS criteria. The proposed poison pill policy update reflects the improving board independence in the market and signals that board independence is critical if a company seeks to deploy a poison pill. It is intended to prevent a non-independent board from arbitrarily using a poison pill mechanism for management entrenchment, particularly when pills are designed for specific shareholders.

Compensation

4. Asia-Pacific Regional markets – Equity Compensation Plans

Current ISS Policy:	New ISS Policy:
<p>General Recommendation:</p> <p>Vote compensation plans on a case-by-case basis.</p>	<p>General Recommendation:</p> <p>Vote compensation plans on a case-by-case basis.</p> <p>For Indonesia, Malaysia, Pakistan, Sri Lanka, Thailand, and Vietnam generally vote for option plans and restricted share plans.</p> <p>Vote against an option plan¹ if:</p> <ul style="list-style-type: none"> ▪ The maximum dilution level for the plan exceeds: <ul style="list-style-type: none"> ▪ 5 percent of issued share capital for a mature company (this may be increased to 10 percent if the plan includes other positive features such as a challenging performance criteria and meaningful vesting periods as these partially offset dilution concerns by reducing the likelihood that options will become exercisable or performance shares are issued unless there is a clear improvement in shareholder value); ▪ 10 percent for a growth company; or ▪ The plan permits options to be issued with an exercise price at a discount to the current market price. <p>Vote against a restricted share plan if:</p> <ul style="list-style-type: none"> ▪ The maximum dilution level for the plan exceeds 5 percent of issued share capital for a mature company or 10 percent for a growth company; or <p>The plan does not include a challenging performance criteria and meaningful vesting periods to partially offset dilution concerns by reducing the likelihood that performance shares are issued unless there is a clear improvement in shareholder value.</p>

Footnotes:

Footnotes:

¹ For Thailand, proposals to issue warrants to directors, executives and/or employees of the listed issuer and its subsidiaries will be treated as stock option grants.

Rationale for Change:

The proposed equity compensation plan policy change will provide clarity on ISS' approach of stock option plans and restricted share plans for companies in Indonesia, Malaysia, Pakistan, Sri Lanka, Thailand, and Vietnam. This addition will also specifically improve clarity for Thailand as the issuance of warrants to directors, executives and/or employees in that market are considered as stock option grants.

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