



UNITED STATES

Information on GICS Changes and Value-Adjusted Burn Rate

Frequently Asked Questions

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This FAQ is intended to provide general guidance regarding the way in which ISS' Governance Research Department will analyze certain issues in the context of preparing proxy analyses and determining vote recommendations for U.S. companies. However, these responses should not be construed as a guarantee as to how ISS' Governance Research Department will apply its benchmark policy in any particular situation.

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1. How should this FAQ document be referenced?

This FAQ document is intended to provide timely information on ISS' plans for addressing forthcoming Global Industry Classification System (GICS) updates and the incorporation of the Value-Adjusted Burn Rate (VABR) factor into the U.S. Equity Plan Scorecard (EPSC). This document supplements the compensation-related FAQ documents that are available on the [Policy Gateway](#). ISS has provided preliminary VABR benchmarks below for informational purposes. The final VABR benchmarks that will apply to shareholder meetings on or after Feb. 1, 2023 will be included in the updated Equity Compensation Plans FAQ document, which is expected to be published in December 2022. If you have questions about this document, please contact the [ISS Help Center](#).

2. How will upcoming GICS changes affect ISS' 2023 pay evaluations?

The S&P Dow Jones Indices and MSCI Inc. have [announced changes](#) to the GICS structure that will be effective March 17, 2023. The announced modifications include GICS grouping changes to retail, data processing & outsourced services, financial services, REITs, and transportation classifications. Most impactful to ISS' processes is the introduction of a new industry group for Equity REITs (6020).

ISS uses GICS classifications for, among other things, peer group construction, pay-for-performance and director pay evaluations, and EPSC purposes. Given the proximity of the expected GICS changes to the 2023 U.S. proxy season, ISS will implement the updated classifications following the June 1, 2023 Quarterly Data Download (QDD). Accordingly, for ISS' pay evaluation purposes noted above, the GICS changes will be effective for shareholder meetings which occur on or after Sept. 1, 2023. For more information on ISS' use of GICS grouping and QDD information, please see the [U.S. Equity Compensation Plans FAQ](#).

3. When will updated burn rate thresholds and SVT benchmarks be provided for the new GICS classifications?

ISS expects to establish new burn rate thresholds for companies affected by the 2023 GICS updates (including companies in the new GICS 6020) in June 2023. These burn rate thresholds will be disclosed following the June 1 QDD and will be effective for shareholder meetings that occur on or after Sept. 1, 2023. ISS also expects to perform new regressions for SVT benchmarks for companies in the new GICS 6020 after the June 1, 2023 QDD is available. For shareholder meetings that occur prior to Sept. 1, 2023, the company's SVT calculations and burn rate benchmarks will be calculated based on legacy GICS classifications.

4. Will the updated GICS classifications be displayed in research reports?

For shareholder meetings that occur following the changes to the GICS structure in March 2023 but prior to Sept. 1, 2023, the front page of the ISS research report may display an updated GICS classification for informational purposes even if the company's legacy GICS classification is utilized for other pay evaluation purposes.

5. What is ISS' Value-Adjusted Burn Rate and how does it compare to the current burn rate methodology?

The new Value-Adjusted Burn Rate (VABR) methodology addresses limitations inherent in the current volatility-based burn rate calculation. The VABR is a more accurate measure of a company's recent equity grant rates through compensation plans, as it uses a methodology that more precisely measures the value of stock option grants. The VABR is based on calculations that are more readily understood and accepted by the market: the actual stock price for full-value awards, and the Black-Scholes value for stock options.

A company's annual VABR is calculated as follows:

Annual Value-Adjusted Burn Rate = ((# of options * option's dollar value using a Black-Scholes model) + (# of full-value awards * stock price)) / (Weighted average common shares * stock price).

For additional information on ISS' burn rate calculations and their role in the EPSC, please see the [U.S. Equity Compensation Plans FAQ](#).

6. When will the burn rate factor for the EPSC change?

Since February 2022, the EPSC has displayed a company's VABR for informational purposes only. As previously [announced](#), beginning with shareholder meetings on Feb. 1, 2023, the U.S. EPSC evaluation will replace the current volatility multiplier-based adjusted burn rate factor with the VABR. At that time, the VABR calculation will be used for the burn rate factor for the U.S. EPSC evaluation and scoring, and the prior volatility multiplier-based burn rate will no longer be displayed.

As a result of this change, ISS will be publishing new benchmarks that pertain to the VABR factor. As in past years, the burn rate benchmarks applicable for the 2023 policy year will be published as an appendix to the annually updated U.S. Equity Compensation Plans FAQ document in December.

7. How will the VABR benchmarks be calculated and is the change expected to significantly affect EPSC scores?

The new VABR benchmarks will appear different from the prior benchmarks due to differing methodologies, and therefore the VABR benchmarks will not be comparable to the prior published benchmarks. The VABR benchmarks are calculated as the approximately 86th percentile of three-year burn rates within the company's two- or four-digit GICS group, segmented by the S&P 500 index, Russell 3000 index (less the S&P 500) and non-Russell 3000 index. In addition, a *de minimis* benchmark threshold has been established separately for each of the S&P 500 index, the Russell 3000 index less the S&P 500, and the non-Russell 3000 index. The *de minimis* thresholds shown in the preliminary benchmarks below will apply to the final benchmarks to be published in December.

While most companies' VABR calculations are expected to change on an absolute basis, the benchmark analysis will continue to compare companies on a relative basis using recent burn rates within a company's industry/index group. As such, the burn rate factor change is not expected to significantly impact EPSC scores. Nevertheless, in order to provide investors and companies a clearer picture as to how the new VABR benchmarks will appear, ISS has included preliminary VABR benchmarks in the Appendix below for informational purposes. However, these preliminary VABR benchmarks are not the final benchmarks that will apply for the 2023 proxy season.

8. Will ISS continue to utilize caps for year-over-year changes to burn rate benchmarks?

Yes, ISS will continue to cap the potential year-over-year changes to the burn rate benchmarks. Under the prior burn rate methodology, year-over-year changes were generally limited to +/- two percentage points. ISS will determine and announce the caps for year-over-year benchmark changes in 2023, after analyzing data from the 2023 proxy season. The caps will apply for the 2024 proxy season.

Appendix: Preliminary Burn Rate Benchmarks for ISS' Value-Adjusted Burn Rate

The below preliminary VABR benchmarks are provided for informational purposes. These preliminary benchmarks are not applicable for the 2023 proxy season and so should not be relied upon by companies. However, ISS anticipates that these preliminary benchmarks will not differ significantly from the final benchmarks that will be published in December 2022 and applicable for the 2023 proxy season.

| S&P500 | | |
|--------|------------------------|----------------------------------|
| GICS | Description | Preliminary Burn Rate Benchmark* |
| 10 | Energy | 0.86% |
| 15 | Materials | 0.77% |
| 20 | Industrials | 0.77% |
| 25 | Consumer Discretionary | 1.22% |
| 30 | Consumer Staples | 0.77% |
| 35 | Health Care | 0.90% |
| 40 | Financials | 0.88% |
| 45 | Information Technology | 1.93% |
| 50 | Communication Services | 1.53% |
| 55 | Utilities | 0.77% |
| 60 | Real Estate | 0.77% |

*A *de minimis* threshold of 0.77% was established for the S&P 500 index.

| Russell 3000 (excluding the S&P500) | | |
|-------------------------------------|------------------------------------|----------------------------------|
| GICS | Description | Preliminary Burn Rate Benchmark* |
| 1010 | Energy | 2.29% |
| 1510 | Materials | 1.34% |
| 2010 | Capital Goods | 1.71% |
| 2020 | Commercial & Professional Services | 2.10% |
| 2030 | Transportation | 1.67% |
| 2510 | Automobiles & Components | 1.96% |
| 2520 | Consumer Durables & Apparel | 2.06% |
| 2530 | Consumer Services | 2.04% |
| 2550 | Retailing | 3.26% |
| 3010, 3020, 3030 | Consumer Staples | 1.74% |
| 3510 | Health Care Equipment & Services | 3.82% |
| 3520 | Pharmaceuticals & Biotechnology | 5.45% |
| 4010 | Banks | 1.05% |
| 4020 | Diversified Financials | 3.64% |

+

| | | |
|-------------|---------------------------------|-------|
| 4030 | Insurance | 1.34% |
| 4510 | Software & Services | 5.47% |
| 4520 | Technology Hardware & Equipment | 4.00% |
| 4530 | Semiconductor Equipment | 3.94% |
| 5010 | Telecommunication Services | 2.90% |
| 5020 | Media & Entertainment | 4.32% |
| 5510 | Utilities | 1.05% |
| 6010 | Real Estate | 1.08% |

*A *de minimis* threshold of 1.05% was established for the Russell 3000 index less the S&P 500.

+ Benchmark based on all companies in the 2-digit GICS due to insufficient number of companies to analyze within the 4-digit GICS.

| Non-Russell 3000 | | |
|-------------------------|------------------------------------|----------------------------------|
| GICS | Description | Preliminary Burn Rate Benchmark* |
| 1010 | Energy | 4.08% |
| 1510 | Materials | 3.96% |
| 2010 | Capital Goods | 4.73% |
| 2020 | Commercial & Professional Services | 4.99% |
| 2030 | Transportation | 3.55% |
| 2510 | Automobiles & Components | 4.45% |
| 2520 | Consumer Durables & Apparel | 4.92% |
| 2530 | Consumer Services | 3.83% |
| 2550 | Retailing | 6.21% |
| 3010, 3020, 3030 | Consumer Staples | 8.72% |
| 3510 | Health Care Equipment & Services | 8.99% |
| 3520 | Pharmaceuticals & Biotechnology | 8.02% |
| 4010 | Banks | 1.23% |
| 4020 | Diversified Financials | 4.12% |
| 4030 | Insurance | 1.70% |
| 4510 | Software & Services | 9.66% |
| 4520 | Technology Hardware & Equipment | 5.57% |
| 4530 | Semiconductor Equipment | 4.83% |
| 5010, 5020 | Telecom & Media | 5.49% |
| 5510 | Utilities | 2.68% |
| 6010 | Real Estate | 2.37% |

* A *de minimis* threshold of 1.23% percent was established for the non-Russell 3000 index.

+ Benchmark based on all companies in the 2-digit GICS due to insufficient number of companies to analyze within the 4-digit GICS.

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