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2025 POLICY UPDATES FROM ISS AND GLASS LEWIS

January 2025

Each year, Institutional Shareholder Services (ISS) and Glass Lewis share updates to their executive compensation voting guidelines, informed by investor and non-investor[1] perspectives. Below we summarize changes effective for the 2025 proxy season. We also review executive compensation topics that were presented as part of the pre-season policy surveys – these items represent design topics to be monitored as they may shape policy changes in the future.

UPDATES TO 2025 VOTING GUIDELINES

Focusing on executive compensation (and related) topics, updates to voting guidelines for the 2025 proxy season are not material. The methodologies to evaluate CEO / senior executive "pay for performance" remain mostly status quo, and nearly all of the perspectives on "best practice" executive compensation design are consistent with past years. Below we summarize the modest changes from ISS and Glass Lewis for TSX Composite Index companies.

ISS	Glass Lewis
Review of Top Executive compensation As part of the pay for performance evaluation, ISS reviews the alignment of CEO disclosed compensation and company performance. New for 2025, in exceptional circumstances, ISS will now have flexibility to review the compensation of a non-CEO named executive officer (e.g., an executive chair or a former CEO) if that would provide a more appropriate assessment of pay-for-performance alignment. **Board gender diversity** ISS will continue to suggest a "withhold" vote for the Chair of the Nominating Committee where women comprise less than 30% of the board membership. Previously an exception was made if a company had 30% women and then fell below 30% due to an "extraordinary circumstance". New for 2025, ISS has removed the need for a disclosed extraordinary circumstance. This change harmonizes the Canadian approach with the US market.	**Problematic pay practices** The ongoing review of executive pay policies allows Glass Lewis to reassess their evaluation of a company's compensation program and amend as necessary. For 2025, Glass Lewis updated its list of "problematic pay practices" to include: • Egregious or excessive perquisites • Adjustments to performance results that lead to problematic pay outcomes As part of the policy update, Glass Lewis confirmed its review of unfavourable factors in a pay program considers the context, overall structure of the pay program, overall disclosure quality, and alignment of pay with performance.

INSIGHTS FROM THE PRE-SEASON POLICY SURVEYS

In 2024, as part of their annual review of voting guidelines around the world, ISS and Glass Lewis each requested investors and non-investors to participate in a survey, collecting feedback on a variety of topics that could inform

[1] Non-investor: a stakeholder, board member, advisor, or issuer of a public corporation.

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future policy changes. Below we summarize the feedback shared by investors and non-investors, noting the feedback is heavily influenced by the US and European markets and not specific to Canada.

INSTITUTIONAL SHAREHOLDER SERVICES

Time-based equity vs. performance-based equity

Historically, investors have preferred performance-based equity as a tool to align the interests of executives and shareholders. However, this preference seems to be shifting, with concerns raised with non-rigorous goal setting, leading to executive pay levels above target and pay-for-performance misalignment. Some stakeholders believe replacing performance-based equity with time-based equity with extending vesting periods (beyond three years) could address the concerns. Survey results suggested investors views are mixed – 43% continue to view time-based equity as problematic, while 31% would support time-based equity with extended vesting as a replacement for performance-based equity. This compares to 70% of non-investors supporting time-based equity with longer vesting periods.

When asked about a preferred vesting period, there was majority support from both investors (66%) and non-investors (58%) for a time frame of at least five years.

Annual incentive programs

ISS views annual incentive programs positively when they are based on quantifiable, pre-set goals with disclosed targets and weights. However, some companies, including large financial sector companies, deviate from market best practices by basing annual incentives entirely on year-end discretionary performance assessments. These companies value a discretionary approach by considering various industry-specific factors, including peer practices, potential risks, and macroeconomic trends. Survey results indicate the majority of investors (52%) oppose the use of discretionary annual incentive programs, even if aligned with peer practices. The views of non-investors are mixed – 38% support discretionary programs, and 31% oppose.

Awards at managed funds

Another concern of ISS is the issue of uncapped fund distributions, which can lead to high reported compensation in niche industries, including alternative asset managers. Such practices are viewed negatively by ISS because these distributions are uncapped, the calculation formula is complex, and the results lead to high reported compensation. Survey responses from investors and non-investors are aligned, with 69% and 46%, respectively, in favour of ISS applying the same pay-for-performance analyses to the distributions of profits from managed funds.

GLASS LEWIS

Equity-based awards

A review of time-based vs. performance-based equity awards was also part of the Glass Lewis policy survey. Despite investors citing concerns with pay-for-performance misalignment and the complexity of some performance-based equity programs, there was consensus that performance-based equity is effective at motivating executives. Investors support time-based equity awards in specific circumstances but continue to prefer performance-based equity.

Disclosure of make-whole awards

As part of executive recruitment, “make-whole” equity grants may be provided to candidates by their new employer to replace equity forfeited on departure from their former company. The policy survey asked about reasonable design

expectations. The majority of investors suggested the grant value should be the same as the value forfeited, the terms of the awards should match (where possible) and the make-whole grants should be time-restricted.

Executive perquisites

Glass Lewis highlights that the value of CEO perquisites is much higher in the U.S. compared to pre-pandemic levels. Survey results indicate that investors views concerns with perquisites as a signal of broader issues with executive compensation governance, justifying against votes if perquisites are excessive (56% of investors). In contrast, non-investors believe concerns with perquisites should be raised through direct engagement, rather than the sole reason for and against Say on Pay vote.

Executive compensation benchmarking

The policy survey covered a variety of topics relating to executive pay benchmarking including peer group design, target pay positioning and engagement with shareholders on material changes. Below we summarize the high-level views of investors, by topic:

- 57% of investors support higher pay levels to attract and retain talent if the company discloses specific details on the competition for talent (evidence-based)
- As part of peer group construction, more than 70% of investors do not support the inclusion of peer companies of a different size or operational scope, egregious pay practice, and significant shareholder opposition; less concern with a different ownership structure
- More than 85% of investors expect companies to seek shareholder feedback prior to (i) meaningful peer group changes, (ii) significant increases to pay levels and (iii) setting a philosophy to pay above median of the peer group
- Concerns with the current “Transatlantic pay gap”, with higher pay levels in the US vs. Europe – majority of investors (60%) consider this problematic. Majority of non-investors (58%) do not see the gap as problematic

ABOUT US

Southlea Group is a national independent compensation advisory firm that provides global perspectives as a GECN Group company working with over 150 compensation professionals in 15 countries. We are headquartered in Toronto with offices in Montreal and Vancouver, and clients across Canada, representing all industries and organization structures. Our team of advisors is multi-disciplined with diverse backgrounds and experiences. We are proud to be a certified Women’s Business Enterprise by WBE Canada and to be Rainbow Registered as an LGBT+ friendly organization.

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