

# MORROW SODALI

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BRAZIL PROXY UPDATES

## PROXY VOTING GUIDELINES UPDATE FOR 2022

ISS and Glass Lewis recently released their policy guideline update for the upcoming 2022 proxy season, effective starting February 1, 2022. Below we highlight material changes<sup>1</sup> relevant for the Americas and Brazil in particular.

The updated guidelines will generally be applied for shareholder meetings taking place in 2022, except for those stated otherwise, with a one-year transition period, which will be effective starting in 2023.

### ISS BENCHMARK POLICY CHANGES FOR ALL MARKETS

To ensure its global voting policies take into consideration the changing views and needs of its institutional investor clients and the broader corporate governance community, ISS gathers input each year from institutional investors, companies, and other market constituents worldwide over a period of many months through a variety of channels. The updates announced on December 6 have been informed by the careful consideration of the many inputs received.

As part of this year's policy development process, ISS undertook a separate dedicated "Climate Survey" to invite feedback relevant to the evolution of both ISS' benchmark and its various specialty policies. It sought input on criteria considered important for determining proper board oversight of climate-related risks, for determining views on regular shareholder votes on climate transition plans, and for assessing the quality of companies' climate transition plans. The Climate Survey also elicited feedback specifically relevant to ISS' specialty climate policy, launched in 2020, which incorporates information and policy approaches using ISS' proprietary climate research. Changes to ISS' specialty climate policy and other specialty policies will be announced in January.

#### BOARD ACCOUNTABILITY ON CLIMATE

Climate change and climate-related risks are now among the most critical topics for many investors, and this area has developed significantly in the last year. Many investors are seeking to better integrate climate risk considerations in their investment, engagement, and voting processes. The policy updates for 2022 introduce a board accountability policy for the assessment of and focus on the world's highest greenhouse gas (GHG) emitting companies. In response to ISS 2021 Climate Survey, a high percentage of investor respondents supported establishing minimum criteria for companies considered to be strongly contributing to climate change.

For 2022, the new benchmark board accountability policy will focus on companies that are significant Greenhouse Gas (GHG) emitters (defined as those on the current Climate Action 100+ Focus Group list). For these companies, ISS will recommend "Against" votes for responsible incumbent directors – usually the appropriate committee or board chair in the first year, dependent on the market – in cases where the company is not considered to have adequate disclosure, such as according to the Task Force on Climate-related Financial Disclosures (TCFD) or does not have quantitative GHG emission reduction targets covering at least a significant portion of the company's direct emissions. ISS will generally vote against the chair of the committee responsible in situations that ISS believes the company is not taking the minimum steps necessary to understand, assess and mitigate the risks related to climate change.

ISS noted that the minimum steps required to mitigate risks should be detailed in the disclosure of climate-related risks, as per TCFD's framework, including:

- Board governance measures
- Corporate strategy
- Risk management analyses
- Metrics and targets
- Appropriate GHG emissions reduction targets

In defining emission reduction targets, ISS states: **For 2022, "appropriate GHG emissions reductions targets" will be any well-defined GHG reduction targets. Targets for Scope 3 emissions will not be required for 2022 but the targets should cover at least a significant portion of the company's direct emissions. Expectations about what constitutes "minimum steps to mitigate risks related to climate change" will increase over time.**

1. Some updates are editorial and do not imply any change in practice. For simplicity, these have not been considered.

### SAY ON CLIMATE (SOC) MANAGEMENT PROPOSALS

ISS is codifying the framework developed over the last year for analysing management-offered climate transition plans put up for shareholder approval, incorporating feedback received during this year's policy development process and from the Climate Survey. For transparency, the policy lists the main criteria that will be considered when analysing these plans (a non-exhaustive list).

ISS will assess management proposals that request shareholders' approval on climate transition action plans on a case-by-case basis, taking into account the completeness and rigor of the plan. Information that will be considered (where available) includes the following:

- The extent to which the company's climate related disclosures are in line with TCFD recommendations and meet other market standards
- Disclosure of its operational and supply chain GHG emissions (Scopes 1, 2, and 3)
- The completeness and rigor of company's short-, medium-, and long-term targets for reducing operational and supply chain GHG emissions in line with Paris Agreement goals (Scopes 1, 2, and 3 if relevant)
- Whether the company has sought and received third-party approval that its targets are science-based
- Whether the company has made a commitment to be "net zero" for operational and supply chain emissions (Scopes 1, 2, and 3) by 2050
- Whether the company discloses a commitment to report on the implementation of its plan in subsequent years
- Whether the company's climate data has received third-party assurance
- Disclosure of how the company's lobbying activities and its capital expenditures align with the company's strategy
- Whether there are specific industry decarbonization challenges
- The company's related commitment, disclosure, and performance compared to its industry peers

### SAY ON CLIMATE (SoC) SHAREHOLDER PROPOSALS

"Say on Climate" shareholder proposals emerged late in 2020 and have increased in 2021, generally asking companies to publish a climate action plan and to put it to a regular shareholder vote. This policy establishes a case-by-case approach toward such proposals, which according to ISS will provide a transparent framework of analysis that will allow for consistency of assessment across markets.

Shareholder proposals put to a vote that request the company to disclose a report providing its GHG emissions levels and reduction targets and/or its upcoming/approved climate transition action plan will be assessed taking into account the following:

- The completeness and rigor of the company's climate-related disclosure
- The company's actual GHG emissions performance
- Whether the company has been the subject of recent, significant violations, fines, litigation, or controversy related to its GHG emissions
- Whether the proposal's request is unduly burdensome (scope or timeframe) or overly prescriptive

### UNEQUAL VOTING RIGHTS

ISS has announced that it will change its policy regarding unequal voting rights starting on February 1, 2023. ISS currently recommends against board members at newly public companies that adopted an unequal voting right structure prior to becoming a public company. Furthermore, such policy is being expanded to include all current public companies with unequal voting rights.

Some exceptions to the policy should be noted:

- Newly public companies with a sunset provision of no more than seven years from the date of going public
- Limited Partnerships and the Operating Partnership (OP) unit structure of REITs
- Situations where the unequal voting rights are considered *de minimis*
- The company provides sufficient protections for minority shareholders, such as allowing minority shareholders a regular binding vote on whether the capital structure should be maintained

ISS also noted this generally includes classes of common stock that have additional votes per share compared to other classes; classes of shares that are not entitled to vote on all the same ballot items or nominees; or stock with time-phased voting rights ("loyalty shares").

## ISS BENCHMARK POLICY CHANGES FOR BRAZIL

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### ELECTION OF MINORITY NOMINEES (SEPARATE ELECTION)

ISS' general recommendation is to vote for the election of minority board nominees (ordinary and preferred holders), as well as minority fiscal council nominees, presented under a separate election when timely disclosure is provided and in the absence of other concerns regarding the proposed nominees. As of 2021, disclosure of minority shareholders' board nominees in a timely manner is now considered market practice.

As such, ISS updated its policy, consistent with current market practice, to clearly state that the lack of timely disclosure of such minority nominees is no longer considered reasonable and will trigger an "abstain" vote recommendation for both the procedural question to request a separate election of a board representative to be elected by minority ordinary and/or preferred shareholders, as well as the actual proposal to elect a minority representative to the board, when no candidate appointed by minority shareholders (ordinary and/or preferred shareholders) is disclosed prior to the meeting.

### INSTALLATION OF FISCAL COUNCIL

In light of the expected improvement of company oversight provided by the fiscal council, given that its members are elected by shareholders and that they have fiduciary responsibilities including the supervision of acts of the company's administrators, ISS currently generally supports the request for the fiscal council installation.

Based on the expectation that fiscal council nominees, appointed by either the company's management or by minority shareholders, should be disclosed in a timely manner prior to the meeting, ISS will recommend voting for the approval of the fiscal council installation and vote to abstain from such proposals in the absence of publicly disclosed candidates.

In the event management recommends against the installation of the fiscal council, vote recommendation will be made on a case-by-case basis.

### BOARD GENDER DIVERSITY

The existing 2021 transitional period language is being removed from the policy as it is no longer applicable. The following gender diversity policy will come into effect starting February 1, 2022:

A negative recommendation<sup>2</sup> will be cast for companies where the post-election board contains no female directors.

- For bundled elections, ISS will recommend voting against the entire slate
- For unbundled elections, ISS will recommend voting against the chair of the Nominating Committee or chair of the committee designated with the responsibility of a nominating committee, or all such committee members if no committee chair has been identified
  - In case no nominating committee has been disclosed, vote against the chair of the board, or the entire board if no board chair has been identified

## GLASS LEWIS BENCHMARK POLICY CHANGES FOR 2022 IN BRAZIL

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### SUPERVISORY (FISCAL) COUNCIL

Glass Lewis has updated its guidelines to clarify that, in the case of controlled companies, the supervisory council should contain at least one undoubtedly independent director and the representation of major shareholders on the supervisory council should not exceed major shareholders' proportional stakes in the company's issued share capital or voting rights.

Glass Lewis maintained that companies without a controlling shareholder should ensure that at least 50% of the supervisory council's members are independent.

### ELECTION PROCEDURES

Glass Lewis has clarified that where they have identified substantial concerns regarding the performance of the board, its committees, and/or individual directors and the board is being elected as a slate, they may recommend that shareholders vote against the entire slate.

### AUDIT COMMITTEE

Based on the assumption that companies should clearly outline the skills and experience of the members of the audit committee, starting from 2023, Glass Lewis may recommend that shareholders vote against the re-election of the audit committee chair of companies listed on the Novo Mercado when they have been unable to determine through the director biographies and disclosure provided by a company that at least one member of the audit committee has proven expertise in corporate accounting matters.

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<sup>2</sup> Glass Lewis specified they do not make voting recommendations solely on the basis of board-level gender diversity in Brazil. This should be a contributing factor in their recommendations on director elections at large cap companies when additional board-related concerns have been identified.

### VIRTUAL MEETINGS

A new section has been introduced into the guidelines to outline Glass Lewis' expectations when companies convene shareholder meetings in a virtual-only format. In particular, they have outlined they look for a robust disclosure in a company's proxy statement that assures shareholders that they will be afforded the same rights and opportunities to participate as they would at an in-person meeting. Where a company fails to provide such commitments in advance of the meeting, Glass Lewis may recommend that shareholders vote against members of the governance committee, or board chair, as appropriate.

### ESG

Glass Lewis outlined they are to evaluate all environmental and social issues through the lens of long-term shareholder value. They strongly believe that companies should be considering material environmental and social factors in all aspects of their operations and that companies should provide shareholders with disclosure that allows them to understand how these factors are being considered and how attendant risks are being mitigated.

Glass Lewis' comprehensive review of its policies on ESG is additionally published in its Proxy Paper Guidelines for Environmental, Social & Governance Initiatives, available [here](#).

Morrow Sodali will continue to monitor changes in ISS policies and how those changes may affect our clients and will keep you informed.

Please contact your Morrow Sodali representative with any questions.

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