Key Considerations for the 2025 Proxy Season

December 18, 2024

The end of the calendar year marks the beginning of the proxy season for many public companies. In this companion to our recent Client Update on Key Considerations for the 2024 Annual Reporting Season, we outline key considerations for public companies preparing proxy statements.

Key Takeaways

- Beginning with the 2025 proxy season, calendar year-end public companies will need to comply with the new equity grant and insider trading disclosures required by Item 402(x) and Item 408(b).

- In light of recent U.S. Securities and Exchange Commission (the "SEC") guidance, companies' pay-versus-performance disclosure should (1) explain the relationship between executive compensation and each company performance metric, (2) disclose GAAP net income as reported in the audited income statement and (3) disclose how company-selected non-GAAP measures used to link executive compensation to company performance are calculated from the audited financial statements.

- Companies should consider whether, in describing the board's leadership structure and administration of risk oversight, it is appropriate to refer to the board's oversight of cybersecurity. If making such disclosure, companies should ensure that it is consistent across their SEC filings and other publicly available information.

- Following an increase in investor focus on artificial intelligence ("AI") in 2024, companies that use or are testing the use of AI should evaluate whether they have an effective, risk-based governance program that will stand up to investor scrutiny.

Regulatory Updates

Equity Grant Disclosure Requirements

Effective for fiscal years beginning after April 30, 2023, calendar year-end public companies must comply with new disclosure requirements relating to stock option awards and stock appreciation right ("SAR") awards granted close in time to a company's release of material non-public information ("MNPI").

- **Narrative Disclosure**. Companies must describe their policies and practices on the timing of option and SAR grants in relation to the release of MNPI. This includes: (1) how the board decides when to grant such awards (for example, whether such awards are granted on a predetermined schedule); (2) whether the board takes MNPI into account when determining the timing and terms of such awards; and (3) whether the company has timed the disclosure of MNPI for the purpose of affecting the value of executive compensation. This disclosure is required regardless of whether grants of stock options or SARs are actually made close in time to the release of MNPI. This disclosure is not required for awards of restricted stock or restricted stock units.

- **Tabular Disclosure**. Companies must provide tabular disclosure of any stock option, SAR or similar option-like award granted to any named executive officer within a period starting four business days before, and ending one business day after, the filing or furnishing of a Form 10-Q, 10-K or 8-K that discloses MNPI (including earnings information but excluding a Form 8-K disclosing only a material new option award grant under Item 5.02(e) of that form). The tabular disclosure must include for each option or SAR: (1) the award's grant date; (2) the number of securities underlying the award; (3) the per-share exercise price; (4) the grant date fair value of each award; and (5) the percentage change in the market price of the underlying securities between the closing market price of the security one trading day prior to and one trading day following the disclosure of MNPI.

Like other executive compensation disclosure, the information required under Item 402(x) may be incorporated by reference into Form 10-K from a definitive proxy statement if the proxy statement is filed within 120 days of the end of the fiscal year.

For more detailed guidance regarding the disclosure requirements under Item 402(x) of Regulation S-K, please refer to our Debevoise Update—SEC Disclosure Requirements for Equity Grants: What You Need to Know for 2024.

Pay-versus-Performance

The 2025 proxy season will be the third year that public companies are required to make pay-versus-performance disclosure under Item 402(v) of Regulation S-K.

At the 56th Annual Institute on Securities Regulation conference held on November 13, 2024, the Staff of the SEC's Division of Corporation Finance (the "Staff") highlighted the following "practice tips" relating to pay-versus-performance disclosure requirements, consistent with comment letters issued by the Division of Corporation Finance on pay-versus-performance disclosure during 2024:

- **Relationships Between Executive Compensation and Company Performance**. In disclosing the relationships between executive compensation actually paid to the CEO and the other named executive officers and the required company performance metrics, companies should explain each relationship in detail as opposed to simply stating the numbers. The pay-versus-performance rules require a clear description (graphically, narratively or a combination of the two) of each relationship.

- **Net Income**. Companies should disclose GAAP net income as reported in the audited income statement, which includes net income attributable to noncontrolling interests.

- **Company-Selected Performance Measures**. If the company-selected measure is a non-GAAP measure, companies should disclose how such measure is calculated from the audited financial statements as required by the rule. A reconciliation of the non-GAAP measure in compliance with Regulation G and Item 10(e) of Regulation S-K is not required.

Comment letters issued during 2024 generally show that the Staff is conducting a close review of pay-versus-performance disclosures, including probing calculations of compensation actually paid. Companies should ensure the numbers reported in the pay-versus-performance table are accurate and the accompanying footnotes and relationship disclosures comply with Item 402(v).

For a detailed discussion on the final pay-versus-performance disclosure rules, please refer to our Debevoise In Depth—Final Pay-versus-Performance Disclosure Rules: Compliance Q&As. Our Debevoise Updates from February 2023, September 2023 and November 2023 describe the Compliance & Disclosure Interpretations published by the SEC since Item 402(v) was finalized.

Insider Trading Policies and Procedures

For public companies with a calendar year-end, compliance with the new disclosure requirements relating to insider trading policies and procedures begins with the 2024 Form 10-K or Form 20-F or related proxy statement.

Under Item 408(b), public companies must disclose whether they have adopted insider trading policies and procedures governing trading in the company's securities by employees, officers or directors, or by the company itself, that are reasonably designed to promote compliance with insider trading laws, rules and regulations and any applicable listing standards. Companies that have not adopted such policies and procedures are required to explain why they have not done so.

Although this disclosure is required by Form 10-K, it may be incorporated by reference from a definitive proxy statement if the proxy statement is filed within 120 days of the end of the fiscal year. However, insider trading policies will still need to be filed as an exhibit to the annual report on Form 10-K.

For more information and recommendations on how to comply with the disclosure requirements under Item 408(b) of Regulation S-K, please refer to our Debevoise In Depth—Key Considerations for the 2024 Annual Reporting Season.

Cybersecurity Disclosure

Although companies are not required to include cybersecurity-related disclosure in their proxy statements, companies should consider whether, in describing the board's leadership structure and administration of risk oversight in the proxy statement, it is appropriate to refer to the board's oversight of cybersecurity. Many companies already take this approach, and those that do should ensure that their cybersecurity risk management and governance disclosures are consistent across their SEC filings and other publicly available information.

Based on our survey of the annual reports filed by 50 S&P 100 companies following the 2023 annual reporting season, we identified the following trends regarding cybersecurity risk management and governance:

- Board oversight of cybersecurity governance generally falls into one of the following three categories: (1) the board has primary oversight; (2) the board has primary oversight with assistance from a specified committee; or (3) a committee or subcommittee of the board has primary oversight.

- Over 25% of S&P 100 companies reported that their boards are updated on cybersecurity matters "regularly," with over 35% of technology companies reporting

that their boards are updated "periodically." A majority used qualitative language to describe the frequency of updates rather than quantitative specificity.

- Most S&P 100 companies cite more than one managerial role as being responsible for cybersecurity risk management.

For more information on best practices regarding cybersecurity disclosures and trends in risk management and governance, please refer to the *Recap of Cybersecurity Disclosures* section in our Debevoise In Depth—Key Considerations for the 2024 Annual Reporting Season.

AI Board Risk Management and Governance

According to an Institutional Shareholder Services ("ISS") survey of S&P 500 companies, approximately 15% of S&P 500 companies disclosed board or committee oversight of AI-related risks, including directors with AI expertise or an AI ethics board, in their proxy statements from September 2022 to September 2023. As the use of AI becomes more prevalent, investors may expect companies in industries that are significantly impacted by AI to include disclosure about board risk management and governance of AI in their proxy statements.

Notably, investor focus on AI increased in 2024, commensurate with increased disclosures by companies regarding their use of or plans to use AI in their business operations. Twelve shareholder proposals relating to AI were submitted as of June 30, 2024, as compared to four in 2023. The proposals generally sought transparency regarding the use of AI in business operations. Most commonly, the proposals requested reports on the use of AI by the company and the anticipated impact of the use of AI, as well as the amendment of the relevant board committee's charter to include AI oversight.

For companies that use or are testing the use of AI, having an effective, risk-based governance program will be important when facing investor scrutiny of AI disclosures, including in light of Glass Lewis's guidelines discussed below.

For further discussion of AI governance considerations, see the Data Blog of our Data, Strategy and Security practice.

Nasdaq and California Diversity Requirements

On December 11, 2024, the U.S. Court of Appeals for the Fifth Circuit issued an *en banc* opinion vacating the SEC's order approving Nasdaq's board diversity requirements. The *en banc* Fifth Circuit found that the Nasdaq diversity rules were "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law" in violation of the

Administrative Procedure Act. This ruling overturns the October 2023 decision by a three-judge panel of the Fifth Circuit that upheld Nasdaq's board diversity rule. Accordingly, Nasdaq-listed companies do not have to comply with Nasdaq's board diversity rules, though a company may choose to continue to disclose board diversity data voluntarily.

In May 2023, the Eastern District of California ruled that California Assembly Bill No. 979 ("AB 979"), which required public companies headquartered in California to include a minimum number of directors from "underrepresented communities" or be subject to fines for violating the statute, violated federal law and was unconstitutional. Additional litigation regarding AB 979 and Senate Bill 826 ("SB 826"), California's gender-diversity statute for corporate boards, is pending. Although the future of AB 979 and SB 826 and their respective compliance deadlines remains uncertain, companies that fall within the scope of such legislation should consider how they plan to comply should such legislation be upheld.

For more information on the Nasdaq and California board diversity requirements, companies should review the *Update on Board Diversity Requirements* section in our Debevoise In Depth—Key Considerations for the 2024 Annual Reporting Season and our Debevoise Debrief—Nasdaq Board Diversity Rule Vacated by Fifth Circuit.

SEC Changes to EDGAR System

Enrollment for the SEC's new EDGAR filer access and account management system ("EDGAR Next") opens on March 24, 2025. Although proxy statements for 2025 annual meetings for calendar year-end reporting companies will not need to be filed through EDGAR Next, companies would be well advised to consider what actions they should take to prepare for EDGAR Next. Companies can prepare for the transition through trialing the beta system, which is currently open and allows testers to use EDGAR Next functions using fictitious data.

All filers will need to have enrolled in EDGAR Next by September 15, 2025. While enrollment opens in March, filers who do not enroll will still be able to file through the legacy EDGAR system until September 12, 2025. Importantly, filers who are not enrolled in EDGAR Next by December 19, 2025 will be required to submit an amended Form ID to access and make submissions on EDGAR, which may result in a delay in filing.

Other Updates

Shareholder Proposal Trends

In 2024, the total number of shareholder proposals received increased slightly from 2023. There were also more no-action relief requests submitted to the SEC than in the previous proxy season. Below is an overview of the shareholder proposal trends from the 2024 proxy season:

- The number of environmental, social and governance ("ESG")-related proposals voted on decreased in 2024 compared to 2023. There were also more ESG proposals that were critical of traditional ESG policies in 2024 compared to 2023.
- There was a significant increase in support for governance-related proposals in 2024 as compared to 2023.
- Very few environment-related and social-related proposals were successful in 2024.
- Investor focus on AI increased in 2024, with 12 proposals related to AI submitted as of June 30, 2024 compared to four in 2023, though such AI-related proposals received low shareholder support, and none passed.

Please see our Debevoise In Depth for more information on the 2024 proxy season—2024 Proxy Season in Review.

Investor Activism Trends

Investor activism increased in the 2024 proxy season as compared to the 2023 proxy season, with board seat contests increasing. However, activists achieved similar success rates as in the past: of the 455 board seats sought by activists as of June 30, 2024, approximately 10% were won, either through a vote or settlement, as compared to 349 seats sought in the comparable period in 2023, of which 12.5% were won by activists. In 2022, activists sought 583 board seats and obtained 14.9% of them. The number of settlements between companies and activists remained steady in 2024.

In 2025, we expect the trends from 2024 to continue and activism to remain elevated. Please see our Debevoise In Depth for more information about investor activism trends from the 2024 proxy season—2024 Proxy Season in Review.

Proxy Advisor Guidance

Glass Lewis made the following noteworthy revisions and clarifications in its 2025 US Benchmark Policy Guidelines, which become effective for shareholder meetings held after January 1, 2025.

- **Board Oversight of AI**. Glass Lewis believes that all companies that use AI should disclose the board's role in overseeing the company's use of AI. This includes disclosing how companies ensure directors have expertise in AI and whether companies are up to date on the issues that can develop from the use of AI. While it is crucial that AI-related issues are overseen by the board, Glass Lewis believes companies should determine whether this oversight can be accomplished by the entire board, a committee or specific directors.

  Glass Lewis will generally not make voting recommendations regarding a company's oversight or disclosure of AI so long as there are no material incidents regarding the company's use of AI. However, if material harm to shareholders results from insufficient oversight and management of AI, Glass Lewis will evaluate the company's AI-related governance practices, the board's response and associated disclosures. If the board's oversight or response to the AI-related issue is not satisfactory, Glass Lewis may recommend voting against the responsible directors.

- **Board Responsiveness to Shareholder Proposals**. Glass Lewis updated its view to reflect that when a shareholder proposal gets noteworthy shareholder support but not a majority (over 30% but less than 50%), the board should speak with shareholders on the issue and disclose shareholders' concerns as well as the board's response.

- **Reincorporation**. When a company proposal involves reincorporating to a different state or country, Glass Lewis will review the proposal on a case-by-case basis. Glass Lewis will review how the reincorporation will impact the company's corporate governance provisions, how legal precedents and statutes in the new jurisdiction will impact the company and the financial benefits the company will receive by reincorporating, as well as other factors resulting from reincorporating in the new jurisdiction.

- **Say-on-Pay**. Glass Lewis clarified that, in evaluating executive compensation, it will take a holistic view and assess each executive compensation program on a case-by-case basis. Unfavorable factors will be assessed in relation to the pay program's entirety and will be evaluated for their rationale, structure and ability to align executive compensation with company performance. For more detailed information on the actions public companies should consider in evaluating their executive

compensation programs, please see our Debevoise Update—2024 Executive Compensation To-Do List for Public Companies.

ISS published the following noteworthy revisions, clarifications and considerations regarding its U.S. voting guidelines in its Benchmark Policy Changes for 2025, which are effective for shareholder meetings held on or after February 1, 2025.

- **General Environmental Proposals and Community Impact Assessment**. ISS updated the factors it will consider when reviewing shareholder proposals for reports on a company's environmental and social policies or the potential environmental and social impact of a company's operations. The factors ISS will consider include: (1) the alignment of current disclosure of applicable company policies, metrics, risk assessment report(s) and risk management procedures with any relevant, broadly accepted reporting frameworks; (2) the impact of regulatory non-compliance, litigation, remediation or reputational loss that may be associated with failure to manage the company's operations in question, including the management of relevant community and stakeholder relations; (3) the nature, purpose and scope of the company's operations in the specific region(s); (4) the degree to which company policies and procedures are consistent with industry norms; and (5) the scope of the resolution.

- **Poison Pills**. ISS clarified the factors that will be considered in the case-by-case evaluation of whether the board's actions in adopting an initial short-term poison pill (with a term of one year or less) without shareholder approval were reasonable, or whether the adoption should be considered a governance failure warranting a recommendation to vote against director nominees. ISS will consider the following factors: (1) the trigger threshold and other terms of the pill; (2) the disclosed rationale for the adoption; (3) the context in which the pill was adopted; (4) a commitment to put any renewal to a shareholder vote; (5) the company's overall track record on corporate governance and responsiveness to shareholders; and (6) other factors as relevant.

- **Special Purpose Acquisition Corporations ("SPACs")**. ISS updated its policy to support requests to extend a SPAC's termination date by up to one year from the SPAC's original termination date (inclusive of any built-in extension options and accounting for prior extension requests). Other factors that ISS may consider include: (1) any added incentives; (2) business combination status; (3) other amendment terms; and (4) if applicable, use of funds in trust to pay excise taxes on redeemed shares.

- **Executive Compensation**. In response to investor concerns regarding performance-based equity compensation programs, ISS is adapting its qualitative review of

performance-vesting equity awards. Effective for shareholder meetings held on or after February 1, 2025, any concerns regarding design or disclosure of performance-vesting equity awards will carry greater weight in ISS' qualitative analysis, and significant concerns will be more likely to trigger an adverse say-on-pay recommendation for a company that demonstrates a quantitative pay-for-performance misalignment. For more information, please refer to Question 34 in ISS' U.S. Executive Compensation Policies FAQ.

Other Practical Tips

Public companies should consider the following practical tips in connection with the upcoming proxy season:

- Consider reevaluating committee responsibilities to address the evolving regulatory landscape. For example, companies should consider the audit committee's role in overseeing cybersecurity disclosure and—if appropriate—climate disclosures and the compensation committee's role in administering clawback policies and overseeing human capital and talent management more broadly. Furthermore, companies should consider addressing these new responsibilities of the audit and compensation committees in their respective charters. Companies that have not already done so should also consider adopting a formal policy governing the timing of equity grants in relation to the release of MNPI in light of the new Item 402(x) requirements.

- Companies should re-evaluate their director and officer ("D&O") questionnaires in light of recent SEC enforcement actions, including the SEC's settled charges against the former Church & Dwight Co., Inc. CEO and Chairman who failed to disclose a close personal relationship with an executive and consequently caused the company's proxy statements to contain materially misleading statements. Companies should consider including questions that prompt disclosure of personal relationships between directors and management that may affect the determination of director independence, confirm the company's internal process for reviewing and flagging follow-up questions to D&O questionnaire responses and consider noting in the cover of the D&O questionnaire that any answers pre-filled by the company must be carefully reviewed by the director or officer. For more information on the SEC's charges, please refer to our Debevoise Digest: Securities Law Synopsis – October 2024.

- Companies may wish to review their compliance programs following the U.S. Department of Justice's (the "DOJ") updated guidance to federal prosecutors addressing how companies manage risks associated with new and emerging

technology, including AI, and expanding on preexisting guidance regarding employee reporting channels, whistleblower protection, post-acquisition compliance integration and use of data for compliance purposes. For more detailed information on the DOJ's updated guidance, please see our Debevoise Digest: Securities Law Synopsis – October 2024.

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Please do not hesitate to contact us with any questions.

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