Corporate Governance and Executive Compensation Trends

May, 2024

Agenda

1

Emerging Corporate Governance Concerns

- Increased Focus on AI and Fracturing of ESG
- Proxy Advisor Vote Recommendations and Investor Voting Trends

2

Overview of Regulatory Updates

- Non-compete Agreements
- Clawbacks
- Proposed Rules
- Options/SARs Grant Timing Disclosures

3

Executive Compensation

- Overview of Current Market Practices
- Looking Forward

4

Q&A

Presented by:

Kip Powell
Associate Partner,
Talent Solutions

Andrew Maletz
Senior Consultant,
Shareholder Engagement

1

Emerging Corporate Governance Concerns

AON

Shifting Governance Risks

Trends — Key Topics to Watch

Board Oversight and Education[1]

- 15% annual decrease in the number of investors supporting issue-expert (i.e., cyber, climate) directors
- More than 80% of investors support topic specific board education, by an external expert, citing higher value from the full board being upskilled

Climate and ESG

- 73% of early filers included climate or ESG risk factors in their form 10-K
- Cited risks included regulatory compliance, impact on profitability or operations, and climate-related extreme weather
- Rising concern that commitments related to ESG could prompt shareholder litigation

Artificial Intelligence (AI)

- 84% of earlier filers included AI-related risk factors, with most keeping the wording and use-cases vague and 'non-substantive'
- First "AI-washing" lawsuit filed against Innodata, and SEC fee penalties issued to two investment advisors, both focused on misrepresentations of the extent to which the company's products and services actually employ AI technology and also the extent of the company's investment in AI

Cybersecurity

- 91% of early filers reference cybersecurity in their form 10-K risk factor section
- Only 36% are providing cyber training to board members; those doing so report higher confidence to respond & comply[2]
- 75% of CISOs are involved in the new SEC breach disclosure process but only 45% of CFOs are involved[2]
  - Creates concern around determination of financial materiality if the main financial controller is not involved

1. EY Center for Board Matters' "2024 Proxy Season Preview"
2. AuditBoard's *'Decode the New SEC Cybersecurity Disclosure Ruling'* report

Governance Considerations: Artificial Intelligence

Trends — Key Topics to Watch

Who is leading **AI as a risk function** and **AI as an opportunity** (operational efficiencies and improvements; how does this impact what the Company sells to clients)?

How are externally-sensitive **Company data assets** being protected from AI being **utilized by third parties and/or in the public domain?**

Does the Company have a **formal AI policy for employees?** Are all **employees aware** of it? How does the Company **assess compliance** with its formal AI policy?

Does the Company proactively and **publicly disclose its AI practices and policies**? If so, is it mentioned in **earnings reports/calls, regulatory filings or supplier agreements?**

Key Considerations

- Clear distinction between the ***policies*** versus the ***controls*** surrounding use of AI
- AI will remain a volatile topic — companies should be cautious of being identified as a leader or laggard, ensuring Directors and Executives are well-equipped to speak to the Company's approach
- Monitor and apply early learning lessons from regulatory fines and litigation externally

ESG Journey Considerations

All companies are at different stages of their ESG journey, there is no one-size-fits-all approach:

- Industry **sector**, **size**, **maturity** and **operating regions** should all be key considerations in determining how to prioritize actions in ESG
- Management should have a deep understanding of evolving ESG risks and their potential impacts
  - Keep senior executives and the Board informed of material topics and the company's progress against goals through a regular cadence
  - Ensure development and implementation of the necessary frameworks to collect and report progress against goals and supporting metrics

The key to success for ESG engagements with financial stakeholders, including insurance companies, should address:

Consistent and compelling messaging across all communication channels

Ensuring **proper oversight and coordination** with management and the board

Prioritizing and reporting on risks and opportunities material to the Company and its peers

Understanding exposure to key datapoints and ratings while being armed with mitigating context for exposure items

Proxy Season Statistics

- Key issues being flagged in SOP reviews:
  - Glass Lewis – Peer Groups & LTI: Increased scrutiny of "oversized" company disclosed peer groups; flagging companies where performance-based LTI is less than 50% of total equity compensation (previously only required 33%)
  - Performance Goal Disclosure: Both proxy advisors noting concerns on the lack of disclosure under annual and long-term plans of goals or metrics, limited disclosure of reconciling non-GAAP performance metrics to GAAP and how payouts were determined – with it only impacting final recommendations when there is poor P4P scoring
- Key Issues Driving Negative Recommendations for Directors:
  - Overboarding: Similar to previous years, overboarded directors are receiving negative vote recommendations from both ISS and Glass Lewis. These concerns from proxy advisors as well as investors are impacting the director vote result – in some cases with support for an overboarded director dropping below 50%
  - Diversity: Glass Lewis and ISS will both recommend against the chair and/or members of the nominating committee due to insufficient gender and/or ethnic diversity on boards, with vote results not dramatically impacted by the recommendations
- Declining Influence of Proxy Advisors?
  - Several high-profile market actors have publicly criticized investors' reliance on proxy advisory vote recommendations, including JP Morgan CEO Jamie Dimon
  - The impact of an ISS "AGAINST" recommendation is declining: In 2020, an adverse ISS recommendation coincided with approximately 35% decline in investor support but in 2024, that has narrowed to approximately 30%

SOP Failures

0.5%

2024 **R3K** failure rate*

2.1%

2023 **R3K** failure rate

3.4%

2022 **R3K** failure rate

SOP Average Vote

92.2%

2024 **R3K** average vote result

90.2%

2023 **R3K** average vote result

Average Director Election Result

95.7%

2024 **R3K** average vote result

94.5%

2023 **R3K** average vote result

*As of May 1, 2024. n=389 meetings.

2

Overview of Regulatory Updates

FTC's Final Rule Banning Worker Non-compete Clauses

On April 23, 2024, the Federal Trade Commission (FTC) issued its **final rule** prohibiting all non-compete agreements for all employees at all levels, with only extremely limited exceptions. This action followed the FTC's January 2023 proposed rule and its review of over 26,000 public comments. The final rule is scheduled to go into effect 120 days after it is published in the Federal Register, which means it is likely to take effect in late August or early September of 2024.[1] The final rule has been challenged by multiple sources and will likely face scrutiny in courts and legal proceedings as it takes effect.

Key Provisions of Ruling:

- **Ban on New Noncompetes**: The final rule prohibits employers from entering into new non-compete agreements with all workers, including senior executives, after the effective date
- **Treatment of Existing Noncompetes**:
  - **Senior Executives**: Existing non-compete agreements can remain in force for senior executives (those earning more than $151,164 annually in a "policy-making position")
  - **Other Workers**: Existing non-competes with workers other than senior executives are not enforceable after the effective date of the final rule
- Violations of the rule will be deemed a violation of Section 5 of the FTC Act, which prohibits "unfair or deceptive acts or practices in or affecting commerce"

Considerations for Companies in light of the New Rule:

- **Review Restrictive Covenants**: Revisit your restrictive covenants, including non-solicitation and confidentiality provisions, to ensure they are reasonably tailored to protect your legitimate interests. Make sure these provisions align with the new rule
- **Assess Necessity**: Evaluate whether the non-compete agreements your company uses are necessary to protect your legitimate interests. Consider alternative mechanisms, such as *non-disclosure* and *non-solicitation agreements*, to safeguard trade secrets and proprietary information
- **Stay Informed**: Keep track of legal developments and any challenges to the rule. Legal proceedings may impact or delay its implementation
- **Provide Notice**: If the rule remains in effect, companies must provide clear and conspicuous notice to workers that their non-compete clauses will not be enforced
- **Trade Secrets Management**: Review internal processes and security measures to prevent unauthorized disclosure

1. Noncompete Rule Summary

SEC Clawback Rule: Corporate Governance Requirement

Clawback Overview — Key Design Features	
WHAT	• Companies are required to recover **"excess" incentive compensation[1] paid based on a misstated financial reporting measure**
WHO	• **Executive officers** • Current and former
TRIGGERS	• Accounting restatement ○ **"Big R" restatements:** corrections of material errors made by restating prior period financial statements ○ **"Little r" restatements:** corrections of non-material errors to previously issued financial statements that would result in a material misstatement if left uncorrected or that are corrected in a current period financial report • Covered person **fault or misconduct doesn't matter**
LOOK-BACK PERIOD	• Incentive compensation paid relating to the **3 completed fiscal years immediately preceding the date of the required accounting restatement**
NO BOARD DISCRETION	• Board is **required to take action** if a restatement triggers a clawback
MISCONDUCT OUTSIDE OF RESTATEMENT	• Not covered by new SEC rule / exchange listing standards • Some companies have separate discretionary provisions or policies to address misconduct and other code of conduct violations
REQUIRED DISCLOSURE	• All companies **must file their clawback policy** as an exhibit to their Form 10-K • If a company has a restatement: (i) must disclose by checkmark (tagging in XBRL) on cover of Form 10-K and (ii) must describe actions taken in the proxy statement
COMPLIANCE DATE	• **Incentive Compensation received on or after October 2, 2023 is subject to clawback and companies will have until December 1, 2023, to adopt a compliant clawback policy**
CONSEQUENCE OF FAILURE TO COMPLY	• **Nasdaq Delisting**

(1) Incentive-based compensation is defined as "any compensation that is granted, earned, or vested based wholly or in part upon the attainment of any financial reporting measure"; time-based equity is excluded, but equity tied to the achievement of TSR or stock price hurdles is included

Regulatory Update

<table>
<tr><th>Status</th><th>Topic</th><th>Update</th></tr>
<tr><td rowspan="2">POTENTIAL RULE PROPOSAL*</td><td>Human Capital Management Disclosure</td><td>September 2023 — the SEC's Investor Advisory Committee (IAC) voted in support of a recommendation that publicly traded companies disclose additional information related to their human capital management practices. The two key pieces of the recommendation include:
A) Enhance quantitative workforce disclosure requirements to be included in the human resources disclosure under Reg S-K Item 101(c). This includes the disclosure of the number of people employed by the issuer disaggregated by employment status (full-time, part-time, etc.); turnover or comparable workforce stability metrics; total cost of the issuer's workforce, broken down into major components of compensation; and workforce demographic data sufficient to allow investors to understand the company's efforts to access and develop new sources of talent, and to evaluate the effectiveness of these efforts.
B) Providing a narrative disclosure in the Management Discussion & Analysis of the 10-K. Further, this recommendation aims to enhance transparency around "how the firm's labor practices, compensation incentives, and staffing fit within the broader firm strategy."
To be considered in the October 2024 meeting.</td></tr>
<tr><td>Corporate Board Diversity</td><td>The SEC may recommend amendments to its disclosure rules to enhance disclosure in filings (including proxy statements) to add information regarding the diversity of board members and nominees. This has now been pushed back on the SEC agenda from October 2023 to October 2024.</td></tr>
</table>

*On April 4th, the SEC issued a stay order for the climate disclosure rules so that the Eight Circuit can evaluate incoming petitions Although the SEC has paused the implementation of the rule while defending it in court, the core provisions related to climate risk disclosures remain in effect.

ORDER ISSUING STAY: In the Matter of the Enhancement and Standardization of Climate-Related Disclosures for Investors

New SEC Disclosure Rule Related to the Timing of Options/SARs

On December 14, 2022 the SEC **finalized amendments to Rule10b5-1** to provide more transparency and prevent trading while individuals are in possession of material nonpublic information ("MNPI"). The rule has multiple disclosure requirements, and one part of the rule, Item 402(x), includes a requirement for both **narrative and tabular disclosure of options and SARs** granted close in time to a company's disclosure of MNPI.

Item 402(x) of Regulation S-K Final Rule
Who needs to disclose and what needs to be disclosed? Item 402(x) applies to US public companies that grant Options or SARs to NEOs. This new disclosure has two elements: narrative and tabular. The narrative element requires all companies to discuss their policies and practices on the timing of options in relation to when MNPI is released. The tabular element will be required only if a company grants stock options or SARs to named executive officers within **four business days before or one business day** after the release of a 10-K, 10-Q, or 8-K that discloses MNPI. The tabular disclosure contains most of the same information required for the Grants of Plan-Based Awards table and adds an additional element: Percentage change in the closing market price of the securities underlying the award between the trading day ending immediately prior to the disclosure of material nonpublic information and the trading day beginning immediately following the disclosure of material nonpublic information. **Where are disclosures required?** Similar to other Item 402 disclosures (e.g., Summary Compensation Table) these disclosures will be required in annual reports on Form 10-K or, if timely incorporated by reference in the 10-k, a company's annual proxy statement (provided the proxy statement is filed within 120 days of the end of the fiscal year.) For most companies, this disclosure will likely appear in the proxy statement for its annual meeting involving the election of directors, as such disclosure may be incorporated by reference into the 10-K. **When will companies first have to disclose?** Companies must disclose for the full fiscal year beginning on or after April 1, 2023. For SRCs, it is the full year that begins on or after October 1, 2023. For all calendar year filers, this means that the disclosure will cover certain grants made during 2024, and any reportable grants will be disclosed in the 2025 proxy statement or 10-K.

3

Executive Compensation

AON

Executive Compensation: Overview of Current Market Practices

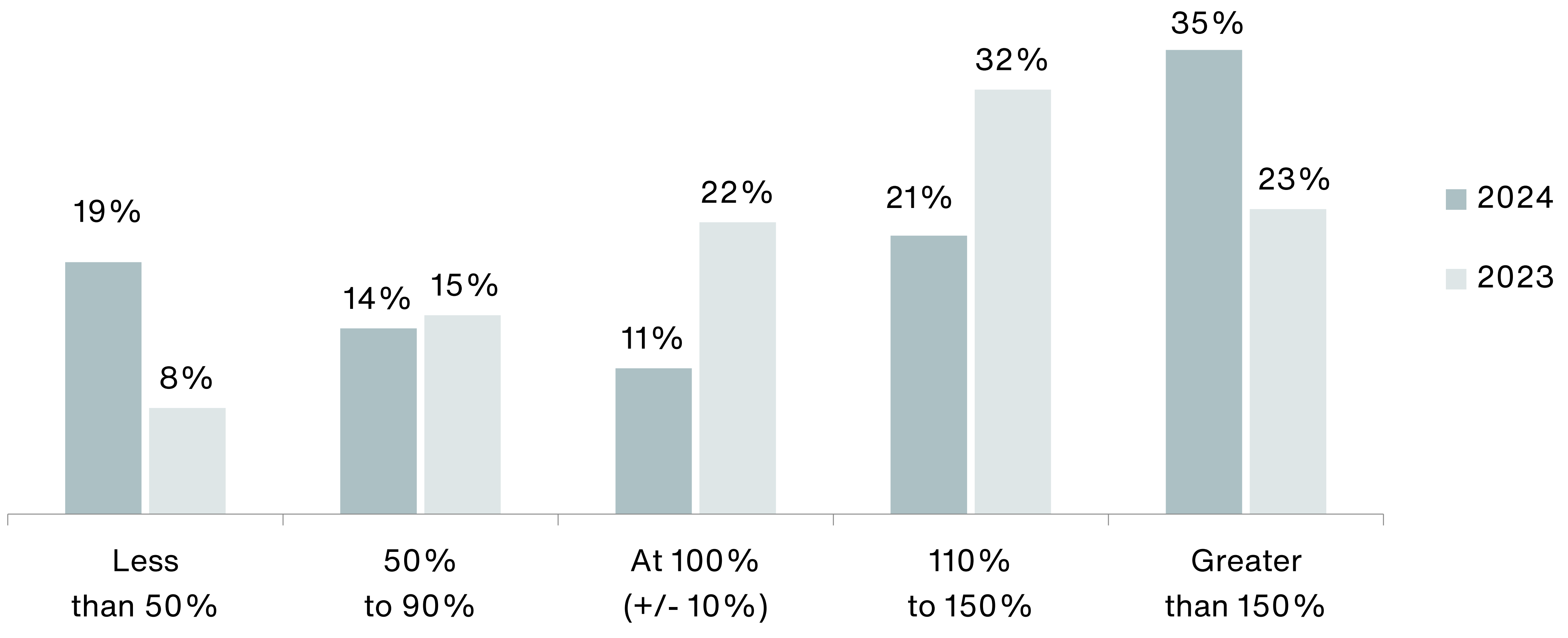
Base Salary

- Projected 2024 budgets per Aon's 2023 - 24 Salary Increase and Turnover Survey (3,500+ U.S. companies)
  - All Industries: 4.0% to 4.5%
  - Approximately 9% indicated 0% budget

Annual Incentives

- Actual payouts in 2024
  - S&P 500 Sample — All NEOs: Paid 119% of target *(median)*
    - *2023 = 116%*
    - *2022 = 150%*

S&P 500 Sample
Distribution of Annual Bonus Payouts (All NEOs)
(% of Target)



S&P 500

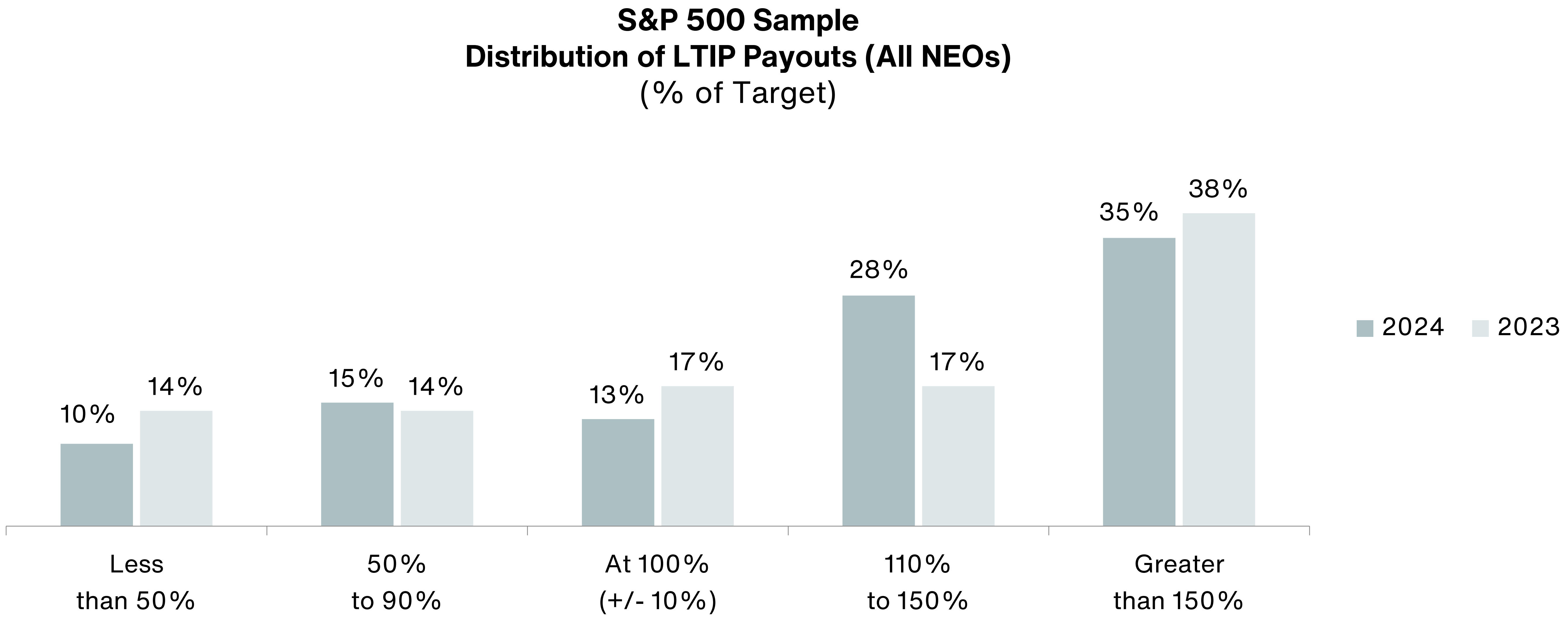
2023 and 2024 payouts

- Over half paid greater than 110% of target award
- 2023 distribution was closer to target than is 2024 (19% paid below 50%)

Executive Compensation: Overview of Current Market Practices

Long-Term Incentives

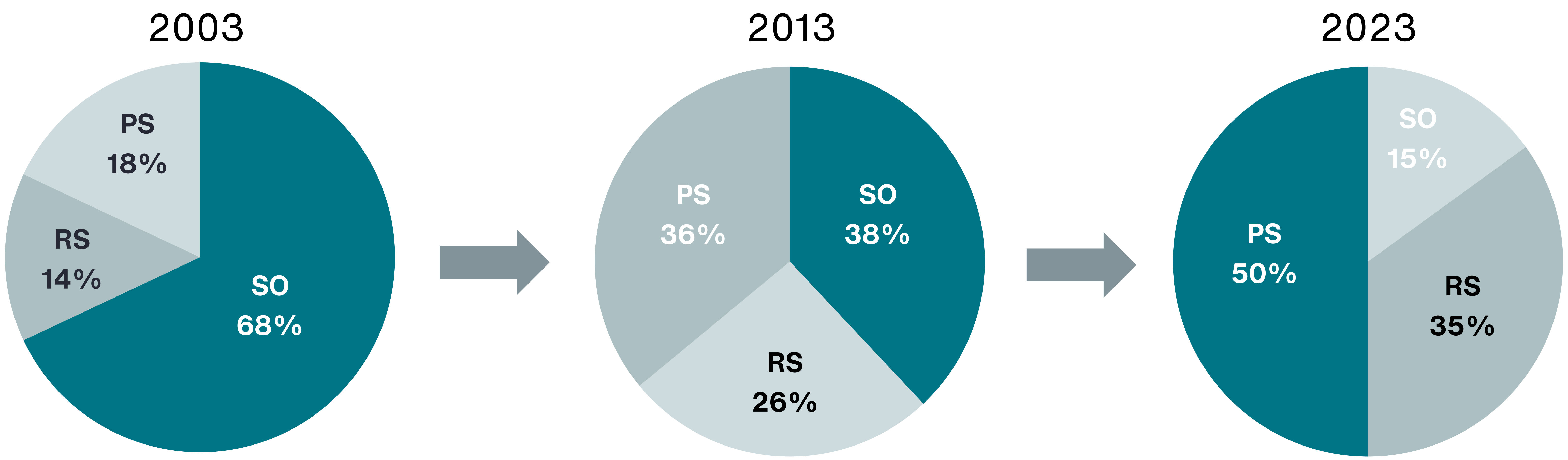
- U.S. companies (S&P 500) tend to offer a balanced portfolio, with highest weight on performance shares
  - Typically, two vehicles with Performance Shares > 50%
  - Prevalence of stock options continues to decline
- Actual payouts in most recent fiscal year
  - S&P 500 — All NEOs: Paid 132% of target *(median)*
    - *2023 = 124%*
    - *2022 = 108%*



S&P 500
<u>2023 and 2024 payouts</u>

- Over half paid greater than 110% of target award
- In 2024 nearly two-thirds paid >110% while in 2023 just over one-half paid > 110%

Executive Compensation: Overview of Current Market Practices



Long-term Incentives Mix — Value Delivered

- S&P 500 Companies
- Shift to performance-based awards over the last 20 years
- ISS requirement for 50% of LTI value to be delivered via a performance-based award

Change Agents

- Stock option expense requirement (2006)
- Enhanced pay disclosure requirements (2007)
- Say-on-pay (2010)
- Shareholder advisory firm influence (ISS & Glass Lewis)
- Pay-for-performance demands of shareholders
- Equity dilution and utilization concerns

Executive Compensation: Looking Forward

Executive Compensation Issues for 2024

- Incentive plan performance ranges
  - Ranges were widened during the COVID years due to financial / supply chain uncertainty
  - Issue: Is it appropriate to go back to pre-COVID ranges (primarily impacting threshold requirements)?
  - Discretion: Increased utilization during COVID years; Did it create bad habits for incentive plan calcs?
- Three-year performance periods for LTIPs
  - Constant struggle for companies to establish 3-year cumulative financial goals
  - Some movement towards a 3-year average performance calculation vs. three separate one-year goals, combined with a cumulative 3-year TSR component
    - 3-year TSR serves as a longer-term market calibration for the internal financial goals
- ESG metrics — Murky future in executive pay plans
  - Used by approx. 75% of S&P 500; Primarily as a reaction to appease shareholders
    - Shareholder question: Are ESG metrics artificially inflating incentive plan payouts?
  - Pendulum swung too far; Swinging back as boards re-examine ESG within incentive plan structure
    - Political backlash and elimination of the term 'ESG' by some companies and institutional shareholders
    - Supreme Court 2023 decision re: race-based college admission 'quotas'
      - Applicability to corporate incentive plans; Risk of litigation if DEI goals are interpreted as 'quotas'

4

Q&A

Any Questions?

Contacts:

Kip Powell
kip.Powell@aon.com

Andrew Maletz
andrew.maletz@aon.com

Thank You

About Us

The Talent Solutions practice at Aon empowers business leaders to reimagine their approach to rewards in the digital age through a powerful mix of data, analytics and advisory capabilities. Our colleagues support clients across a full spectrum of needs, including compensation benchmarking, pay and workforce modeling, and expert insights on rewards strategy and plan design. To learn more, visit: rewards.aon.com.

About Radford

Radford is part of the Talent Solutions practice at Aon and specializes in providing compensation data and advice to technology and life sciences companies. To learn more, visit: radford.aon.com.