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Say on Pay 2022 Overview & Outlook

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Say on Pay votes for 2022 have all been cast and tallied in what represented a down year in Say on Pay results for both the S&P 500 and Russell 3000 constituents. Despite the easing of the pandemic throughout 2021, economic uncertainty lingered amid inflation and continued sociopolitical concerns. For many companies, human capital concerns persisted forcing Compensation Committees and company leadership to navigate the retention of critical talent and employee incentivization. Compensation actions that accomplish these goals are not always viewed favorably from an external perspective, which the recent downtick in Say on Pay results indicates. As highlighted below, larger companies tend to recognize this impact sooner and to a greater extent than smaller companies.

2022 Say on Pay Overview

The S&P 500 and Russell 3000 saw reduced levels of shareholder support for executive pay in 2022, with averages falling for each index; however, the S&P 500 had less severe declines across the board. One-third of S&P 500 companies had below 90% support in both 2021 and 2022 and the 4.2% fail rate is also flat year-over-year. In contrast, the Russell 3000 saw a greater percentage of companies with support levels below 90% and companies failing their vote than in the prior year. Both groups are towards the lower end of historic ranges[1] of support for Say on Pay, and the S&P 500 continues to fall under greater scrutiny, as would be expected.

Say on Pay Vote Results	S&P 500			Russell 3000		
	2021		2022	2021		2022
Average Level of Support	87.8%	→	87.2%	90.1%	→	89.2%
% of Companies with <90% Support	33.3%	→	33.3%	26.5%	→	28.2%
% of Companies Failing (<50% Support)	4.2%	→	4.2%	2.8%	→	3.5%

While receiving low support on the Say on Pay vote in any given year, or consecutive years, is not ideal, it is also not uncommon to expect this to happen at some point in a company's history. Approximately 17% of S&P 500 companies have failed a Say on Pay vote at least once, with only 3.5% failing multiple times. Further, just over 40% of companies in the S&P 500 have received less than 70% support at least once in their history. This outcome is frequently a result of companies' significant pay actions (e.g., one-time, special equity grants) and/or down cycles from a performance perspective (e.g., stock price). There is a similar trend in Say on Pay support levels for Russell 3000 companies, although not as pronounced, as a lower percentage of companies is present in each case (detailed below), again highlighting the increased investor focus on larger companies.

Say on Pay Vote Results	Failed at least once	Failed multiple times	<70% support at least once	<70% support multiple times
S&P 500	16.7%	3.5%	41.7%	20.2%
Russell 3000	13.4%	3.2%	35.1%	15.7%

Proxy Advisor Impact

Institutional Shareholder Services ("ISS") is recommending 'Against' for slightly more companies than in previous years. Of S&P 500 companies, 11.9% received 'Against' recommendations in 2022 compared to 11.5% last year. For the Russell 3000, the year-over-year increase was more pronounced, with 13.7% of companies receiving 'Against' recommendations this year compared to 11.4% last year. Also, average levels of support for companies receiving an 'Against' recommendation declined year-over-year, consistent with the trend among all companies across both indices. The average support level for S&P 500 companies with 'Against' recommendations fell from 56.2% to 54.0%, while average support level among the Russell 3000 fell from 62.9% to 62.1% which further demonstrates the general theme of increased impact and scrutiny on larger companies.

ISS Against Recommendation	S&P 500			Russell 3000		
	2021		2022	2021		2022
% of Companies	11.5%	→	11.9%	11.4%	→	13.7%
Average Level of Support	56.2%	→	54.0%	62.9%	→	62.1%

While the higher percentage of companies with 'Against' recommendations in the Russell 3000 relative to the S&P 500 is a change from last year - the percentage of companies was roughly equal between indices in 2021 - this outcome is more in line with the ten-year average from 2011 to 2021[1]. Over that period, average support levels for companies with 'Against' recommendations were higher in the Russell 3000 than the S&P 500, consistent with the 2022 results.

ISS recommendations significantly impact the level of support a company receives. Among companies whose year-over-year recommendations went from 'For' to 'Against', which characterizes most companies receiving an 'Against' recommendation, average support dropped 39% in the S&P 500 and 34% in the Russell 3000. For companies that received consecutive 'Against' recommendations, the average year-over-year change in support is mixed, with the S&P 500 increasing by 3% and the Russell 3000 decreasing by less than 1%. This difference could be the result of larger companies having more resources dedicated to investor outreach efforts.

ISS Against Recommendation	Average Change in Level of Support	
	'For' → 'Against'	'Against' → 'Against'
S&P 500	-39.0%	+3.1%
Russell 3000	-33.9%	-0.9%

1 Say on Pay: 10-Year Landscape and 2021 Expectations (https://www.capartners.com/cap-thinking/say-on-pay-10-year-landscape-and-2021-expectations/) highlights the history of Say on Pay vote results since its inception in 2011.

Future Expectations

In 2023, Say on Pay results are likely to be shaped by the unique sociopolitical and economic environment companies face today, the impacts of which have not been felt equally across industries. Amid the threat of recession and a tight labor market, many companies felt obligated to take special actions during 2022 for retention purposes, as stock price declines due in part to the Fed's anti-inflationary measures negatively impacted executives' equity holdings. Shareholders and proxy advisors may not view such actions as favorably as in previous years if paired with dramatic drops in stock price, especially towards year-end, given the potential for misalignments in pay-for-performance. Similarly, some companies may trigger pay-for-performance concerns in cases where above-target bonus payouts based on strong financial metric performance for most of 2022 are coupled with year-end share price decreases. Companies in hard-hit industries, such as technology and financial services, may also draw increased scrutiny from the proxy advisors over their efforts to reign in COVID-era overexpansion with sweeping layoffs. However, as in previous years, we expect pay-for-performance misalignment to continue to be the main driver for 'Against' recommendations from proxy advisors in the broader market.

Conclusion

Despite various external headwinds and continuing uncertainty in the environment in which most companies are operating, last year saw more of a return to pre-COVID levels in Say on Pay vote results. However, recent changes to the regulatory landscape are beginning to influence upcoming proxy statements[2], giving investors additional information to digest and potentially act upon. As we've seen over the history of Say on Pay, changes in disclosure requirements and evolving governance practices take time to influence vote results. Therefore, we expect the ripple effect of such changes on Say on Pay voting in 2023 to be muted, and that many of the same trends experienced this year will continue.

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2 SEC Issues Final Rules for Pay Versus Performance Disclosure (https://www.capartners.com/cap-thinking/sec-issues-final-rules-for-pay-versus-performance-disclosure/) gives an overview of the new SEC required pay versus performance disclosure.