Responsible Investment Report 2020

Interim report

Rathbones
Look forward

Responsible Investment Report 2020

Interim report

In this report we have provided a summary of our stewardship activities for the period January to June 2020.

Please note, we provide more detail in our annual responsible investment report, published in the Spring. That report also gives information relating to our policies and practices around responsible investment.

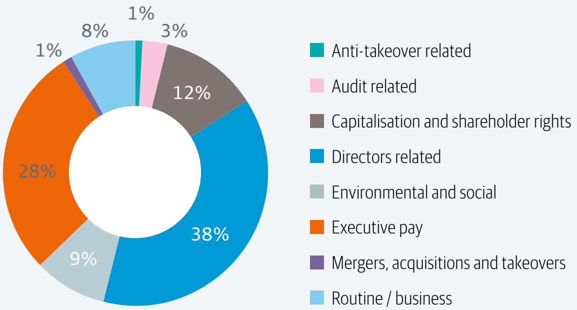
Voting activity

2020 voting (Jan-Jun 2020)

Category	Number	Percentage
Number of items voted	4,883	
Number of votes FOR	4,709	96.44%
Number of votes AGAINST	202	4.14%
Number of votes ABSTAIN	43	0.88%
Number of votes WITHHOLD	7	0.14%
Number of votes on shareholder proposals	123	2.52%

Note: The data provided are in summary form for general information about voting trends and do not reflect the specific votes entered at a specific company. For example, given our status as a private client asset manager with very close links to our clients, it is entirely plausible (if not frequent) for us to enter three different votes for each voteable item, or some combination of For / Against / Abstain. Hence the numbers of items voted For, Against and Abstain would not be expected to add up to the total number of resolutions on which we voted, as we may have entered multiple separate votes for a single resolution.

Votes against management



Votes against management

Anti-takeover related	2
Audit related	7
Capitalisation and shareholder rights	28
Directors related	85
Environmental and social	20
Executive pay	62
Mergers, acquisitions and takeovers	3
Routine / business	19

Engagements in the period

Here we provide more detailed examples of the types of engagement we pursued in the first half of 2020 across a range of environmental, social and governance (ESG) topics.

Note: Please be aware that our engagement activities cover our entire holdings, across all client accounts. The inclusion of a company in this list does not necessarily mean that a particular Rathbones client holds that stock.

Environmental:

Barclays:
Issue: At the 2020 AGM, the board put forward a resolution which, if approved, would allow Barclays to become the first net-zero emissions bank. A potential barrier to this ambition was the fact that Barclays remained the largest fossil fuel financier in Europe and the sixth largest globally. As such, a separate shareholder resolution by ShareAction was also put forward at the AGM requesting that the company commit to phase out the provision of financial services to companies within the energy and utilities sector(s) that are not aligned with the Paris Agreement.

Process: We engaged with Barclays in a meeting coordinated by the Institutional Investors Group on Climate Change (IIGCC) to understand the position of management towards both climate resolutions. We also had a separate dialogue with the proponents. Given these were some of the most important resolutions put forward in this AGM season, our approach was debated by our head of research, chief investment officer, the Responsible Investment Committee, Stewardship Committee and Engagement Working Group. It was agreed that we would support management on their resolution to become a net-zero bank by 2050 but that we would also support ShareAction's climate resolution calling for the phasing out of fossil-fuel financing.

Outcome: Barclays' climate resolution was supported by 99.93% of shareholders. The reason this resolution gained such a high level of support was because it was management backed. The ShareAction resolution gained 23.95% support. Although this resolution failed to pass, it gained over 20% support meaning that Barclays was placed onto the Investment Association 'Public Register'. This is a publicly available register where all votes gaining over 20% opposition against management are placed. The company will be required to speak to shareholders and provide a response as to how it has taken on shareholder feedback within six months. We have since spoken to ShareAction to provide our own insight as to what worked well and the next steps ahead of the 2021 AGM.

ExxonMobil Corporation:

Issue: The company has historically lagged its peers on the issue of climate action and shown an unwillingness to respond to the climate agenda. In particular, we note the company's failure to disclose its carbon footprint and to set binding emissions reduction targets. In 2019, the company called on the US Securities Exchange Commission to block a shareholder resolution which would have called on the company to adopt and disclose greenhouse gas emissions. Climate change requires the company to make serious changes to its climate strategy in order to align with the Paris Agreement and to ensure long-term value creation. We felt that the board had consistently failed to listen to growing concerns by shareholders on the danger that climate change poses to the company's operations.

Process: We chose to issue a split vote on the re-election of the chairman, who also holds the role of CEO. We felt such a move was necessary by shareholders to ensure that climate change becomes a strategically important area in the board's thinking. That said, one of our fund managers chose to support management, as they felt the company would benefit from stability during the ongoing COVID-19 pandemic. We also chose to support the shareholder resolution calling for an independent chairman and the separation of the roles of CEO and chairman. The team felt that this resolution was likely to gain far higher levels of support from shareholders than a director vote against the chairman.

Outcome: 7% of shareholders voted against the re-election of the chairman. Although there was not enough opposition to defeat their re-election, it was notable as the first time we have voted against the re-election of a director based on a company's lack of response to the climate crisis. Legal & General and BlackRock also took similar positions and voted against the chairman. The resolution calling for an independent chairman had 32% support. We expect this resolution to be raised again at the 2021 AGM.

Chevron Corporation:

Issue: Some of Chevron's main lobbying partners including the Chamber of Commerce, American Petroleum Institute and National Association of Manufacturers have been ranked as some of the biggest opponents of the Paris Agreement. It could be argued that a failure to align lobbying activities with the Paris goals presents a real reputational, legal and operational risk to a company. Chevron's membership of these lobbying groups appears to be at odds with the company's stated position of support towards the Paris Agreement. These groups represent significant obstacles to progress in addressing the climate crisis.

Process: We chose to support the shareholder resolution calling on the board to clearly disclose how the company's direct and indirect lobbying aligns with the Paris Agreement. We felt that improved transparency of the lobbying activities was in the best interest of shareholders.

Outcome: This resolution gained 53% support. This was one of the highest levels of support for a shareholder climate resolution seen during the 2020 AGM season. In the US, any shareholder resolution which gains over 50% support is passed, however these resolutions are not binding and the company does not have to implement any changes should it not wish to do so. That said, the board will struggle to ignore such high levels of shareholder support amid the changing attitude of shareholders towards climate change.

Social:

Pfizer:
Issue: Understanding the gender pay gap is crucial for improving equality between men and women and closing the pay gap. The UK has regulation in place requiring companies with more than 250 employees to publish gender pay gap statistics. In the US, the regulations in this area are less stringent. While Pfizer meets the high standards of reporting required on its UK workforce, Pfizer does not publish for its US or global workforce the same 'unadjusted' gender pay gap statistic as is published in the UK. This is the median pay gap statistic (as opposed to equal pay statistic), which is a better figure for demonstrating how well women are represented across a business. Diversity is a key governance concern at the companies in which we invest, with evidence demonstrating that more diverse boards can lead to outperformance. That being the case, we consider disclosure of metrics like the gender pay gap to be important in ensuring good management of social risks.

Process: Our bespoke voting policy is supportive of proposals calling for improved transparency on a company's gender pay gap. This is a standard position we take as a group. As such, we decided to support the shareholder resolution calling on the board to report on its gender pay gap and the actions it is taking to reduce the impact.

Outcome: The shareholder resolution gained over 36% support. Although this failed to pass, it is a useful indicator to the board that shareholders wish to see improved reporting and disclosure on the global median pay gap. We will continue to encourage the board to adopt better standards of reporting to minimise the risk to our investments brought about by companies demonstrating poor practice towards gender equality.

Altria Group:
Issue: Research from the Centers for Disease Control and Prevention (CDC) found that in 2018, 78.2% of middle and high school students had been exposed to e-cigarette advertising, and approximately 20% of high school students were now consuming e-cigarettes. While Altria Group have taken a strong stance to discourage smoking by those that are underage, the company recently acquired a large stake in Juul, a company which currently owns around 75% of the US e-cigarette market. At Altria Group's AGM, a shareholder resolution was put forward requesting that the board report on the policies it has in place to discourage the use of nicotine products among young people.

Process: We decided that it was in our clients' best interests to support this resolution. It was felt that improved reporting by the board would reassure shareholders that this is a priority issue for the company, especially given that the company is facing ongoing federal investigations and lawsuits in this area. We wrote to the company ahead of the AGM to signal our reasons for supporting. A review of the policies in place to prevent underage tobacco use and the effectiveness of these policies would give shareholders greater understanding of how the company is managing this risk.

Outcome: The resolution failed to pass but gained 35% support. This is an encouraging level of support; however, the situation remains unchanged and this will continue to be a key risk to the company given the growing reputational and legal risks to companies found to have insufficient policies in place to protect the young. We expect a similar resolution of this nature to be put forward at the 2021 AGM and we will look to continue our discussions with the company at the next available opportunity.

Governance:

Informa:
Issue: A new provision of the 2018 UK Corporate Governance Code calls for pension contribution alignment between executive directors and the wider workforce. The Investment Association has also specifically mentioned that it expects remuneration committees to set out a credible action plan to reduce the pension contributions of incumbent directors to align with the majority of the level of the workforce by the end of 2022 or risk further shareholder dissent. Under the proposed renumeration policy at the 2020 AGM, the CEO was in line to receive pension contributions of 30% base salary, with the wider workforce due to receive 5%. There is a risk in the current climate that variations in pension contributions of this magnitude could exacerbate tensions between staff and senior management and potentially undermine morale, with a detrimental effect on the operational culture.

Process: We wrote to the chairman ahead of the AGM to inform the board that we would be voting against the remuneration policy and to signal our dissatisfaction with the current arrangements. This is a position we take at all companies where pension contributions are not aligned and no intention has been given to align contributions by 2022.

Outcome: 42.9% of shareholders voted against the remuneration policy. This was one of the largest votes against a remuneration policy during the UK AGM season. We were disappointed with the response from the board as they seemed to suggest that because company performance had been strong, high pension contributions were justified. We felt the board had not grasped the severity of the issue. Variable pay in the form of an annual bonus and long-term incentive scheme is in place to reward an executive director for outperformance, not pension contributions. We notified the board that investors and proxy advisers will continue to flag this issue until the pension contributions of the executive directors are aligned with the wider workforce. A few months later, we wrote to the remuneration committee chair ahead of a consultation to discuss the AGM results. We reiterated our position and called for the alignment of pension contributions to meet best practice guidelines.

Lloyds Banking Group:

Issue: The ongoing COVID-19 pandemic has brought an added risk when approving binding pay arrangements. It is often not clear whether there will be a sustained impact on businesses and how companies will be positioned in a post COVID-19 world. Guaranteeing a greater proportion of executive remuneration (as opposed to variable and/or performance-related renumeration) poses a significant risk to shareholders if company performance were to fall during this period. At the Lloyds AGM, the remuneration policy, if approved, would increase the guaranteed elements of pay for executive directors from 33% to 71% of total pay opportunity. In addition to this, the new policy would introduce a non-performance-based scheme instead of a performance-based long-term incentive structure.

Process: We spoke with the investor relations team at Lloyds to gain a better understanding of the arguments put forward by the company. Following this discussion, we spoke with our external proxy voting adviser ISS to gain their insight as to whether a vote against was the appropriate stance to take. After further discussion with the Rathbones Stewardship Committee and with the company, we chose to vote against the remuneration policy and the item to approve the new long-term incentive plan. We asked the board to increase the percentage of executive remuneration deemed at-risk. We believe it is crucial that the board continue to create pay arrangements that properly align the incentives of senior management with the experiences of shareholders and incentivise behaviours that guarantee the long-term health of the company. We felt that the proposed arrangements risked causing a divergence between the potential experiences of shareholders and senior management.

Outcome: Both items passed but suffered shareholder revolts, with 36% of shareholders voting against both items. The company has been placed on the Investment Association 'Public Register'. The company is at risk of reputational damage should it fail to take on board shareholder concerns. We will be looking to engage at the next meeting with the company. We are anticipating a number of issues with pay arrangements will present themselves in the coming year, as the full impact of the pandemic is known. In particular, we plan to pay close attention to companies who did not apply discretion to pay arrangements despite making use of various government support schemes.

Netflix:

Issue: The board of Netflix has a history of failing to implement changes which have received majority support from shareholders. Since 2012, over 20 shareholder proposals have received majority support and yet most have not been implemented by the board. In 2017, the resolution on the adoption of a simple majority for future resolutions (instead of a supermajority) received support of 63.5%, rising to 88% in 2019. At the 2019 AGM, the four directors up for re-election received support from between 32.6% and 47.1% of shareholders and yet no changes were made. It is incumbent on the board to apply changes to governance arrangements when approved by shareholders in order to minimise the risks to shareholders and the company. This approach taken by the board deviates from recognised best practice and is at odds with what is seen throughout the S&P 500.

Process: This was the first time we had voted at the company's AGM. Once we were familiar with the history of the board and its lack of responsiveness, we felt it was necessary to abstain our vote for all the board members up for re-election. We felt a vote against at the first time of asking would have been too severe; however, we did not feel confident that the board had done enough to warrant our support.

Outcome: The CEO, who also holds the role of chairman, received 33% opposition, as did one of the non-executive directors who was up for re-election. The senior independent director however received over 50% opposition to their re-election. This was the first time we had seen this during our voting on the US AGM season and we fully expect the board to make changes as a result, especially considering the high levels of shareholder opposition in general to director re-election.

Principles for Responsible Investment (PRI) engagements

In the first half of the year we have been involved in a number of ESG-themed engagement projects as part of this initiative.

Responsible sourcing of cobalt

Rathbones continued its ongoing engagement with Microsoft, focusing on their responsible sourcing practices around cobalt in line with OECD Due Diligence Guidance. Rathbones has been involved in several calls with senior figures at Microsoft to better understand how they are addressing the issue of responsible sourcing of cobalt and to encourage them to improve specific practices. How the company is managing its cobalt supply chain during the COVID-19 pandemic is also a key focus area.

Votes against slavery

In 2020, Rathbones convened an investor collaboration with £3.2 trillion in assets under management to challenge FTSE 350 companies that had failed to meet the reporting requirements of Section 54 of the Modern Slavery Act 2015. We worked with a respected international NGO to develop a target list of companies, our aim being to achieve full compliance from 22 laggard companies. We expect members of the FTSE 350 to lead in this area, taking substantive action against the prevalence of slavery in their supply chains. As at the end of September 2020, 18 out of 22 companies have now become compliant. Our engagement was shortlisted for the PRI 2020 Awards for the 'Stewardship Project of the Year.'

Airlines and aerospace companies on climate change

Rathbones are a signatory to the investor statement focusing on airlines and aerospace companies and what they should do to manage their climate change risks and opportunities. The PRI, in consultation with investors engaging airlines and aerospace companies via Climate Action 100+ (of which Rathbones is a member) has developed investor expectations as guiding standards to support companies in managing their climate-related risks and proactively positioning themselves for the transition to a low-carbon economy.

COVID-19 and the pharmaceutical sector

Rathbones signed an investor letter to the largest global international pharmaceutical companies calling on the pharmaceutical sector to take action in this time of crisis. We believe that the pharmaceutical sector has a pivotal role to play in providing effective solutions for COVID-19 in a productive and responsible way. Rathbones chose to be the lead investors for the engagements with Abbott Laboratories and AstraZeneca.

Find It, Fix It, Prevent It

Rathbones signed up to a new engagement in June 2020 calling on businesses in the hospitality sector to find victims of slavery within their supply chain and support their rehabilitation. We want companies within the hospitality sector to develop better policies, processes and procedures for tackling modern slavery. Rathbones is the lead investor for the engagement with Mitchells & Butler and supporting investor for the engagement with Greggs.

Business group CEOs' resilient recovery letter

Along with 120 UK companies, Rathbones signed the letter sent to the Prime Minister asking that the UK economic recovery plans being developed align with the UK's wider goals and deliver a clean, just recovery, that creates quality employment and builds a more sustainable, inclusive and resilient UK economy for the future.

Sustainable recovery letter to EU leaders

Similar to the letter sent to the British Prime Minister, we signed a letter sent to EU leaders ahead of the European Council meeting in July. This called for an economic recovery that includes maintaining momentum on the Green Deal, sustainable finance and an ambitious 2030 greenhouse gas emissions reduction target, with at least 25% of the EU's long-term budget contributing to climate objectives. The letter received support from 178 investors representing more than €12 trillion in assets.

Investors, migrant labour, modern slavery and COVID-19

This engagement has been organised by CCLA Investment Management through Find It, Fix It, Prevent It, which we mentioned above. This engagement will encourage companies operating in the UAE to assist with the identification and then the provision of remedy (particularly the reimbursement of recruitment fees and costs) to migrant labourers who have been released from their roles due to the COVID-19 outage. It is our understanding that many of the promised and existing roles have been revoked and that large numbers of workers who have already travelled are being returned to their home countries leaving many with significant levels of debt that will be impossible to repay. This is likely to lead to increased levels of suicide, other social harm, and potentially – due to the impact of the illness – overwhelm local public health systems.

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Look forward

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