Rathbones

2022: a year of resolutions and revolts

Rathbones Group Voting Season Review 2022

Some thoughts from the stewardship team

If you had asked us, a few years ago, for the best metaphor for the voting season, we might have been tempted to suggest a rubber stamp of monumental proportions, next to a large barrel of ink.

However, the voting season, when shareholders vote on how companies are run, who is in charge and how much they are paid, has changed considerably since then.

The best metaphor now would probably involve a microscope.

The days of shareholders simply supporting management almost without thought are thankfully behind us. This year saw, for instance, shareholder revolts over executive pay (notably GlaxoSmithKline) and climate change (Glencore). It also saw the increasing use of ESG (short for environmental, social and governance) 'shareholder resolutions'. These add up to a way for shareholders to present their own agendas to management and other shareholders. They were used with particular success in pushing for company-wide audits of whether men and women, and people of every ethnic group, are being treated fairly.

We cover all these issues in separate sections in this voting review, which looks at votes at both annual and extraordinary general meetings (AGMs and EGMs). Although this review covers only the first six months of 2022, the voting season, which takes place between April and June, includes the majority of European and US company AGMs each year.

How voting works

Voting is governed by different laws, depending on the country. However, at a basic level, shareholders have a say in who is managing the company and how they are paid, in addition to other governance arrangements designed to protect shareholder interests. Votes can be binding or advisory.

These days, votes cover an increasing number of environmental and social issues, as well as governance. We have defined standards for a range of ESG topics and these form part of our voting policy. This is because ESG factors are integral to the business strategy and operational performance of companies and therefore have the potential to impact outcomes for shareholders. We also recognise the benefit to considering ESG in the context of the potential long-term effect of corporate practices on the continuing health of the overall economy and society, as outlined in our document, 'Responsible capitalism'.[1]

Voting by a single investor seldom brings about sweeping changes to company behaviour overnight. However, it is a powerful statement through which, bit by bit, shareholders can mould the corporate landscape for the better.

1. rathbones.com/knowledge-and-insight/responsible-capitalism-benefiting-society-and-investment-returns

Voting is one of our four core principles of responsible investment

ESG integration

We consider environmental, social and governance (ESG) factors in the evaluation of investments, to help identify ESG opportunities and risks.

Voting with purpose

We actively vote across over 95% of the value of our holdings[2] in line with our responsible investment commitments. This may involve voting against management to help drive positive change.

Engagement with consequences

We will prioritise engagement[3] where we can make a real difference in addressing the world's systemic environmental and societal challenges. We are prepared to reduce our holdings in companies that continue to present an ESG risk over time.

Transparency

As a prominent participant in financial markets, we are committed to being transparent about our approach to responsible investment. We will actively report on the progress of our responsible investment activities to our clients, shareholders and other stakeholders.

2. Percentage covers votable assets only.
3. We also prioritise engagement regarding non-ESG issues that may be material to investor outcomes.

Executive pay

"For investors, it is right that executives are rewarded for doing well for shareholders over the long term."

The issue

It is in the interest of investors that talented people bringing specific skills to tough, demanding roles should have an incentive to perform and be rewarded for their achievements. But the appropriate size and nature of the reward has been a topic of debate for decades. For example, when executive pay starts to climb out of step with average wages, companies risk reputational damage and low morale, which is bad for shareholders.

Our voting policy only approves pay arrangements that reflect a thoughtful consideration of how best to reward executives for the creation of sustainable growth over a longer period (usually three years). In the UK, that's done through a binding vote on a pay policy at least every three years and an annual advisory vote on how that policy was applied.

Salary is just part of the equation for senior executives. They can expect an annual bonus, a long-term incentive scheme - a reward, usually in shares, for achieving particular performance goals over a more protracted period (usually three years) - and generous pension provisions. These all need careful monitoring by investors. It's important that management is incentivised to do well for both shareholders and society.

What happened in 2022

Overall pay for chief executives in the FTSE 100 has reached a median of £3.6 million, according to Deloitte's '2022 AGM season update', similar to the level struck in 2018 and near the record high of £4 million in 2017. Deloitte found that the median FTSE 100 chief executive earned 81 times the average UK employee, compared with 59 in 2020 and 75 in 2019.

A major feature of pay reports in the last year was that most executives' annual bonuses were paid out at near to the maximum possible. This reflects, in some cases, changes to previously agreed performance targets following the interruption from the pandemic. Bonus structures in hospitality companies such as pub chains, for example, were rendered obsolete by the prolonged economic lockdown. This meant that executives couldn't meet financial targets. However, in some cases, the reset targets looked undemanding.

The level of payouts and the sense of the ease with which they were achieved triggered some big votes against management in the UK.

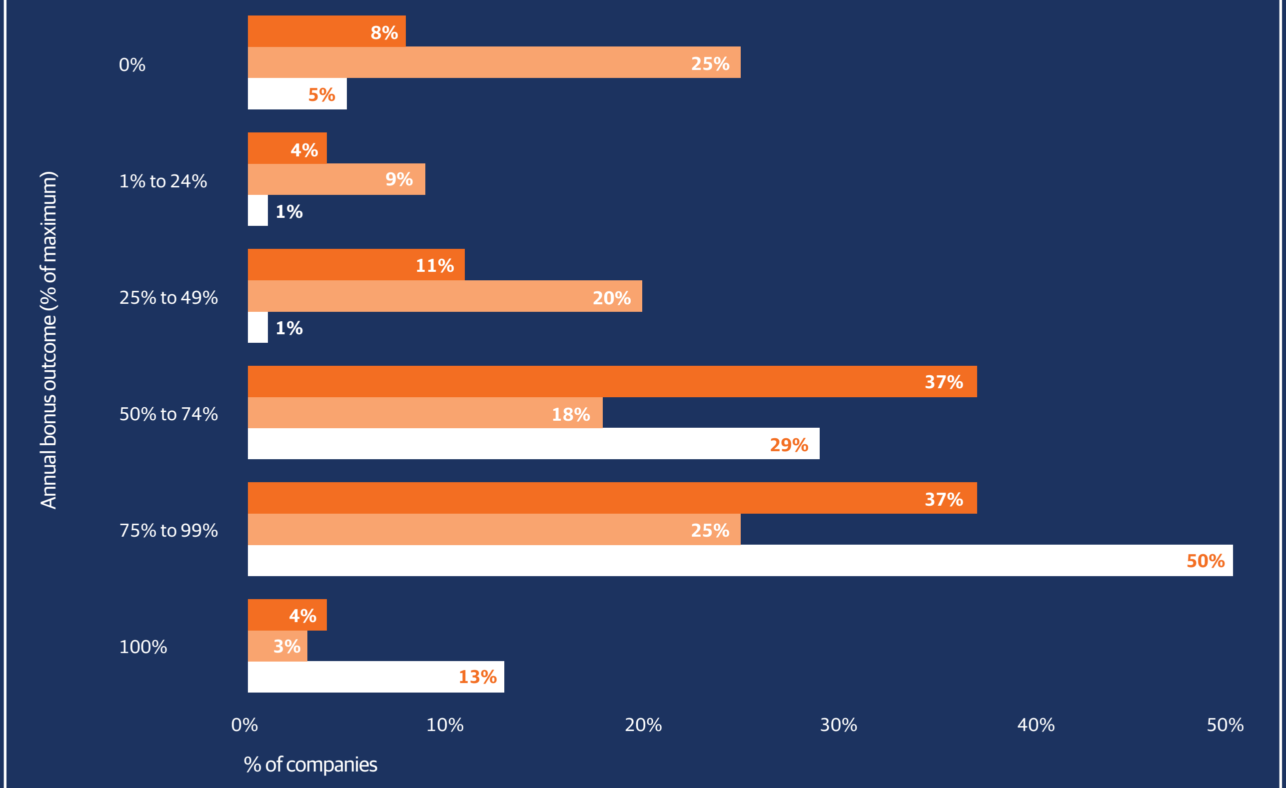
Median pay for chief executives in FTSE 100

£3.6 million

What we did in 2022

We have voted against bonus awards and long-term incentive schemes for companies that either used pandemic-related payment facilities offered by the UK Government or laid people off in 2021, while failing to reduce awards to below the maximum of what the payout terms allowed. We also considered whether the company had failed to pay a dividend and whether shareholder returns had fallen during the reporting period. For these reasons, we targeted Whitbread, Capita, Johnson Service Group and SSP Group. We engaged with these companies, asking them to show discretion by reducing the awards to below what the terms permitted.

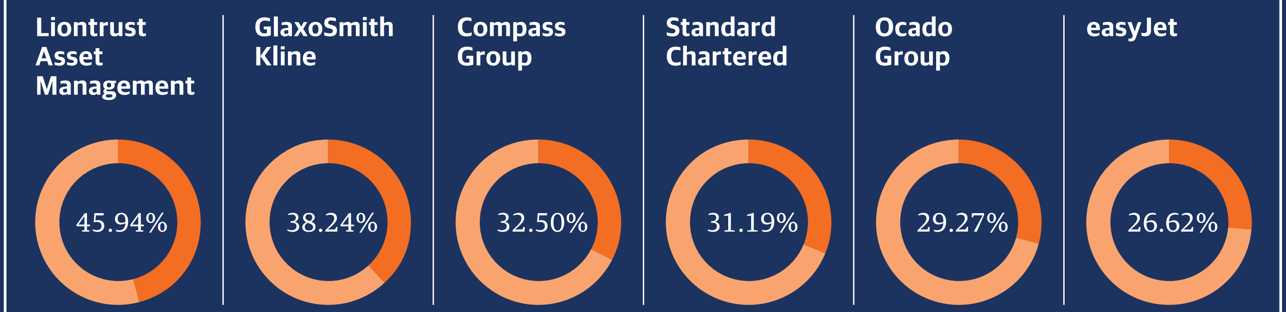
Annual bonuses for FTSE 100 CEOs surged closer to maximum payouts in 2021



Due to rounding not all numbers total 100
Source PwC: Full report can be found at www.pwc.co.uk/services/human-resource-services/insights/executive-pay-ftse-100-mid-agm-season-update.html
Table contains most recently published data

Criticism of top executive pay triggered big shareholder revolts against pay policies at many UK companies

% of votes against pay



Source: Rathbones

Diversity

> "We believe that increasing diversity on boards helps create the best conditions for a strong corporate culture."

The issue

For investors, diversity makes sense. Research shows that companies with executive teams that have strong gender and ethnic diversity are more likely to outperform their more uniform peers on measures such as profitability. This reflects studies that suggest a diverse group of people may make better decisions.[4]

We believe that increasing diversity on boards helps create the best conditions for a strong corporate culture. For example, we think boards that lack diversity are missing a valuable opportunity to bring in voices that represent a wide range of potential and actual clients. More diverse boards may also reduce groupthink, where the board can adopt a single point of view rather than considering different scenarios and strategies.

We know we need to do our part in increasing diversity on company boards. As with executive pay, circumstances vary by region, but the UK has two main government-backed targets. The Hampton-Alexander Review calls for FTSE 350 companies to set a minimum target of 33% female representation. The Parker Review target is for each FTSE 100 board to have at least one director from an ethnic minority background.

What happened in 2022

In 2021, FTSE 350 companies had appointed a record number of women to their boards. The year also saw great improvements in ethnic diversity on FTSE 350 boards.

In the course of our engagement, we found that as of June 2022, 317 FTSE 350 companies had met the Hampton-Alexander target, up from 220 in 2021 and 53 in 2015. However, any sense of complacency that corporate Britain is moving rapidly towards equal numbers of men and women at the top should be checked when we reflect on the length of time companies have had to attain this level.

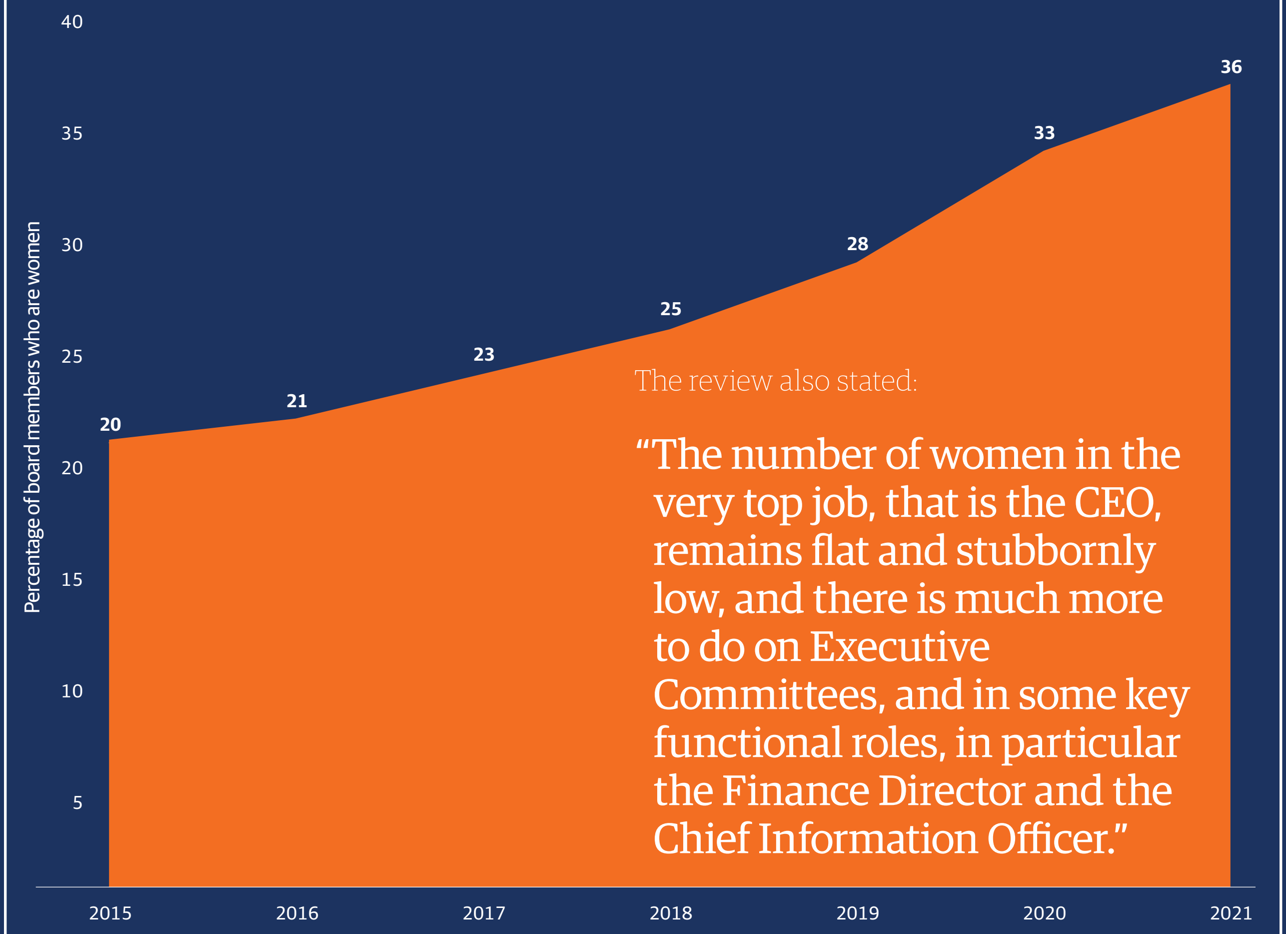
317

FTSE 350 companies met the target of 33% female representation on boards in June 2022.

In March 2022, the government-led FTSE Women Leaders Review set a new end-2025 voluntary target for FTSE 350 companies of 40% for board positions and leadership teams. In the EU, boards will in effect be mandated to meet a 40% quota for women (or men if they're in the minority) as non-executive directors by mid-2026, with 33% for all directors. Non-executive directors don't run the company day-to-day but have a role in overseeing the company is run.

4. See, for example, mckinsey.com/featured-insights/diversity-and-inclusion/diversity-wins-how-inclusion-matters and hbr.org/2016/11/why-diverse-teams-are-smarter

The proportion of women on FTSE 350 boards is rising steadily



The review also stated:

"The number of women in the very top job, that is the CEO, remains flat and stubbornly low, and there is much more to do on Executive Committees, and in some key functional roles, in particular the Finance Director and the Chief Information Officer."

Source: Heidrick & Struggles analysis of BoardEx data on the full board composition of FTSE 350 companies

Almost half of FTSE 350 companies have no woman in a critical leadership role

Source: Heidrick & Struggles
'Critical leadership roles' include Chair, senior independent director, CEO and chief financial officer (CFO)

What we did in 2022

At the start of 2022, we wrote to 74 FTSE 350 companies that had less than 33% female representation and 17 FTSE 100 companies that had no ethnic or racial diversity at board level.

By the beginning of June 2022, 41 of these FTSE 350 companies had achieved 33% female representation and 12 of the FTSE 100 companies had an ethnic minority director.

For the remaining recalcitrant companies, we voted against the re-election of the nomination committee (NomCo) Chair (or Chair of the board if no such position exists) where a company had failed to meet the target by the time of its AGM. However, we took a more lenient approach, abstaining rather than opposing, in two circumstances. The first was where a company had said when it would meet the target. The second case was where a company lacked diversity because of genuinely extenuating circumstances, such as the surprise resignation of a board member who was either female or from an ethnic minority. The NomCo selects board candidates and evaluates board members' performance.

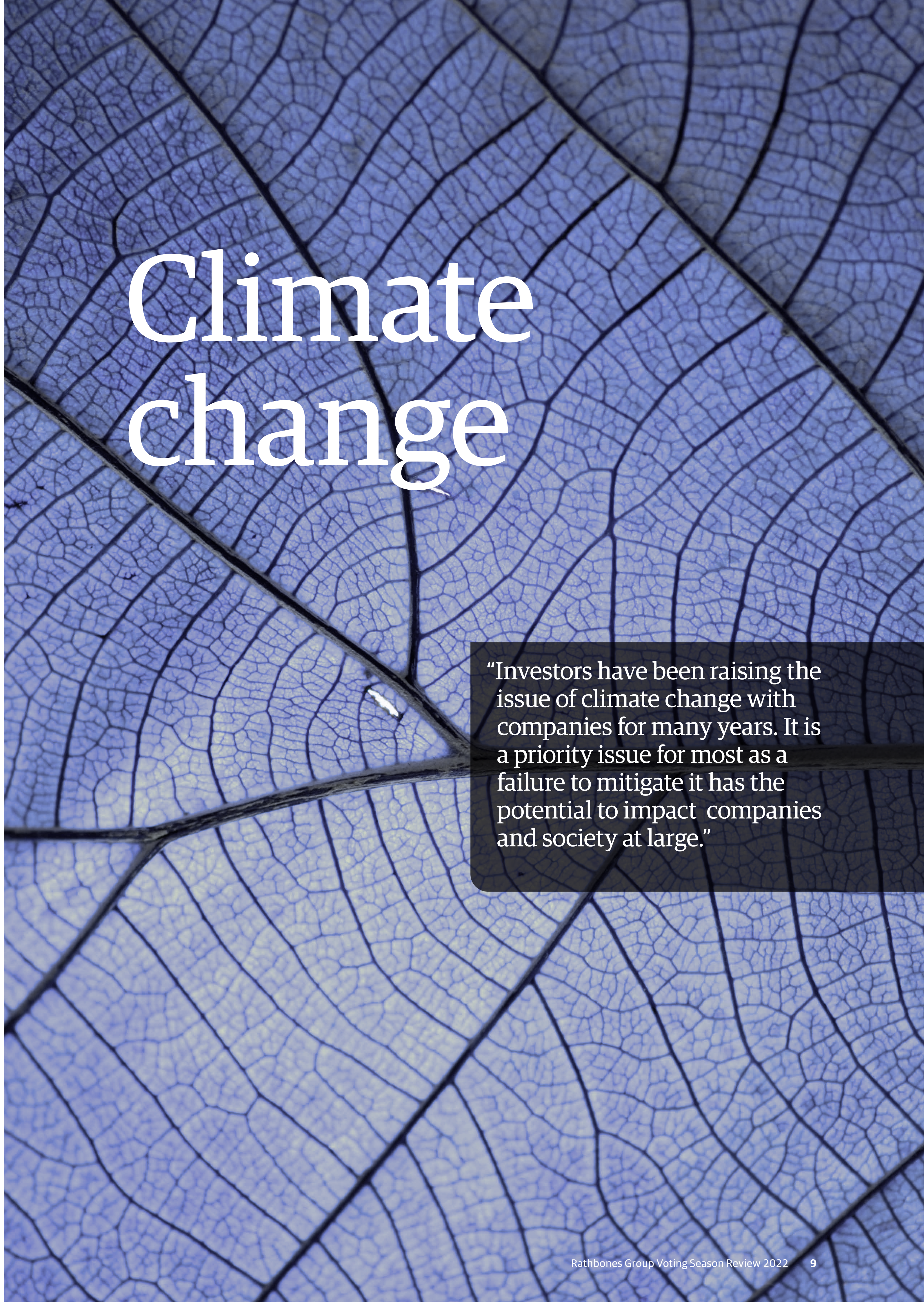
For example, at Great Portland Estates' AGM, we abstained on the re-election of the NomCo Chair because a female non-executive director was stepping down after the AGM, temporarily reducing the proportion of women on the board from 36 to 30%.

However, we do expect boards to have adequate talent management systems that don't leave them high and dry should a female and/or ethnic minority director suddenly resign.

Using the NomCo, we challenged FTSE 350 companies with a poor gender balance

Company	Female representation at time of AGM	Vote against nomination committee Chair	Rathbones' stance
Antofagasta	30%	5.5%	Abstain
BAT	30%	6.2%	Abstain
Bunzl	29%	9.6%	Abstain
Hikma Pharmaceuticals	30%	31.0%	Against
Rolls-Royce Holdings	31%	0.3%	Abstain
Ocado Group	23%	6.8%	Against
Rio Tinto	30%	2.2%	Abstain
Weir Group	27%	4.4%	Abstain
Whitbread	30%	11.3%	Abstain
XP Power	25%	4.1%	Abstain

Source: Rathbones



Climate change

"Investors have been raising the issue of climate change with companies for many years. It is a priority issue for most as a failure to mitigate it has the potential to impact companies and society at large."

The issue

Awareness of the threat from climate change is arguably at an all-time high; so too is the global ambition to fight it. Now that China and India have set net zero targets - in India's case at Glasgow's COP26 Climate Summit in 2021 - some 83% of global emissions are covered by net zero targets.[5] But important work remains in realising that vision - and no more so than in the corporate world. The investor-led Climate Action 100+ engagement initiative, of which Rathbones is an active member, presses 166 companies responsible for 80% of global industrial greenhouse gas emissions to take the necessary action on climate change. The Net Zero Tracker, an alliance of non-profits and academics, estimates that more than one-third of the world's largest publicly traded companies now have net zero targets, up from one-fifth in December 2020. However, it asserts that the majority of these targets need to be more robust.[6]

Investors have been raising the issue of climate change with companies for many years. It is a priority issue for most as a failure to mitigate it has the potential to impact companies and society at large. One increasingly common way of doing this is through voting. Over the last 18 months shareholders have pushed companies to present them with a regular report on how the companies plan to achieve their own net zero ambitions: 'Say on Climate' votes. We've also seen co-ordinated votes to remove directors deemed not to be taking climate risk seriously. Finally, shareholders are now asking the auditors questions. This last element is important for shareholders, as we rely on their work to give us a clear and fair picture of the current and future health of our investments. Our engagement here (in collaboration with others) has focused on making sure that auditors are stress-testing financial reports against appropriate future scenarios. A great deal of climate-related work is also done through shareholder resolutions; we discuss these in the next section.

Companies with Say on Climate votes include miners, energy companies and banks

Company	Shareholder resolution	% support
Anglo American	Advisory vote to approve the Climate Change Report	94.2%
NatWest Group	Approve NatWest's Climate Strategy	92.6%
BP	Approve Net Zero – From Ambition to Action Report	88.5%
Standard Chartered	To endorse the Company's net zero by 2050 pathway	83.0%
Rio Tinto	Climate Action Plan	82.1%
Barclays	Approve Barclays' Climate Strategy, Targets and Progress 2022	80.8%
Shell	Approve the Shell Energy Transition Progress Update	79.9%
M&G	Approve Climate Transition Plan and Climate-Related Financial Disclosure	79.6%
Glencore	Approve Climate Progress Report	76.2%

Source: Rathbones

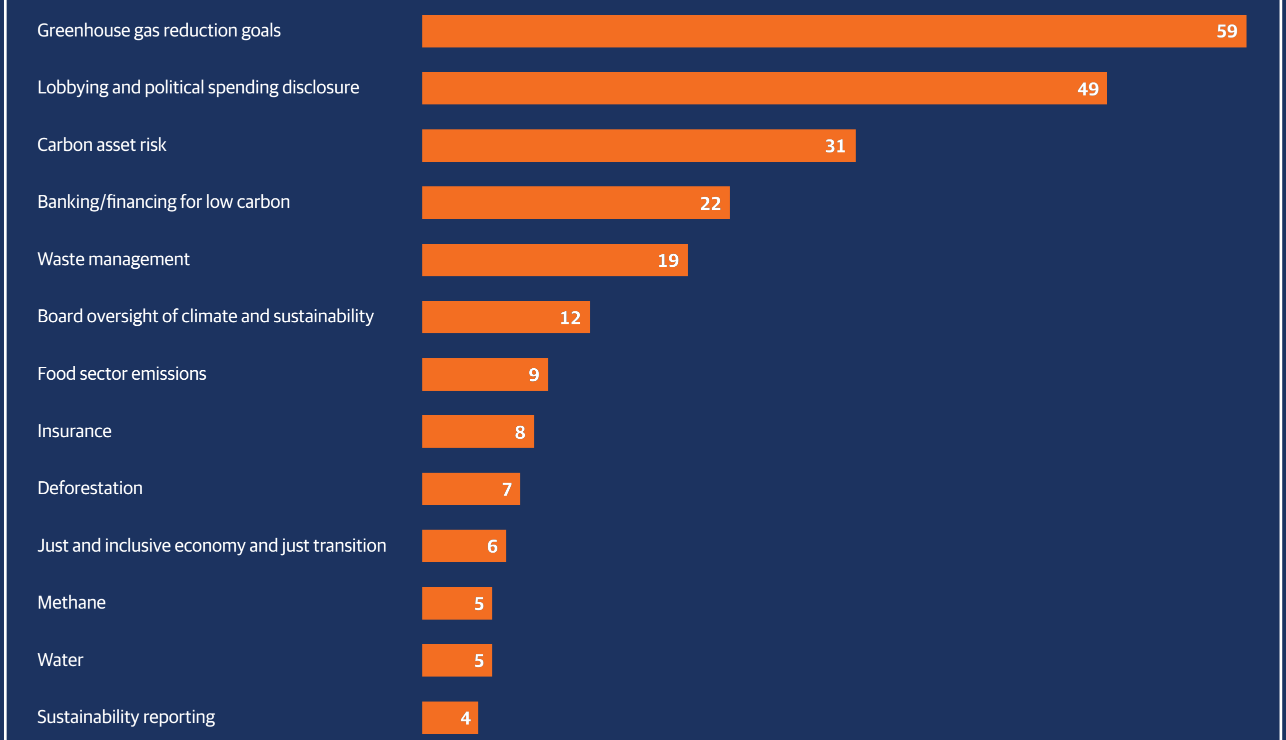
5. netzeroclimate.org/innovation-for-net-zero/progress-tracking/
6. zerotracker.net/analysis/net-zero-stocktake-2022/

Many directors were targeted for inaction and opacity over climate change

Company	Targeted directors	% opposition
Bunge	Kathleen Hyle	5.6%
Chevron	Michael Wirth / Ronald Sugar	7.6% / 12.8%
Valero Energy Corporation	Joseph W. Gorder / Robert Profusek	10.7% / 10.9%
Marathon Petroleum	Evan Bayh	10.8%
ConocoPhillips	Ryan M. Lance / Robert Niblock	7.1% / 7.8%
Exxon Mobil Corporation	Ursula M. Burns / Darren W. Woods	10.9% / 8.9%
Goldman Sachs	Ellen Kullman / Mark Winkelman	5.3% / 4.8%
Berkshire Hathaway	Warren Buffett / Susan Decker / Ajit Jain	4.6% / 13.4% / 4.4%
Wells Fargo	Celeste Clark / Maria Morris	5.9% / 6.4%
Total SA	Jean Lemierre / Maria van der Hoeven / Lise Croteau	6.5% / 6.6% / 5.5%

Source: Rathbones

Shareholders filed a wide variety of climate-related resolutions in 2022



Source: Ceres

What happened in 2022

A record number of companies tabled 'Say on Climate' votes in 2022. These votes typically ask shareholders to assess the companies' detailed plans for, decarbonising, their businesses: reducing emissions, investing in solutions to climate change, and so on.

Counter-intuitively, perhaps, the large degree of shareholder dissent for many of these resolutions - almost a quarter of Glencore shareholders, for example - is quite encouraging. It sends the message that companies simply must do better in this area because investors aren't just rubber-stamping anything a company says.

The US market also saw a major upswing in efforts to express, through votes against incumbent board directors, concern over poor-quality climate disclosure and action. Although it was rare for these votes to reach much above 10%, even these relatively small votes against sitting directors signify a new approach - and one that looks likely to gain ground in the coming years.

What we did in 2022

Back in 2021, we established clear criteria for assessing corporate Say on Climate plans on our website. We have continued to use these in 2022. Whilst not amounting to an automated scorecard, this framework helps us make sure that we only approve plans where all relevant areas are covered in detail.

The most common area where we have concerns about corporate climate plans is in the reach of the targets: do they cover Scope 3 emissions? This means the emissions generated both in companies' supply chains and when their products are used. Overall, all the major fossil fuel companies still have a long way to go in producing rigorous plans for fighting climate change.

We have clear criteria for judging companies on climate change

Governance

Board oversight of the management of climate change risks

Position on climate lobbying that doesn't conflict with the Paris Agreement

Strategy

Net zero commitment by 2050 (or sooner) backed by interim targets consistent with the Paris Agreement and verified by the Climate Action 100+ Net-Zero Company Benchmark. This benchmark is a way of assessing how well companies are making the transition to a net zero world

Planning for different climate scenarios, based on different assumptions of how the climate will change

Metrics and targets

Targets are science-based (verified by the Science Based Targets initiative, a non-governmental organisation) and absolute basis – not "we will cut emissions by 10% for every dollar revenue" but "we will cut emissions by 10%"

Targets encompass Scope 1, 2 and 3 emissions (different kinds of emission for which companies are directly or indirectly responsible), calculated in a credible way

Risk management

Future capital spending in line with greenhouse gas reduction targets, including the year in which investment in carbon-intensive assets, such as oilfields, is expected to peak

ESG shareholder proposals

"Shareholder resolutions are effective in showing investor concern on very specific issues. These prompt management to focus on these problems."

The issue

Our rights as shareholders don't end with voting. We also have the capacity, in certain countries at least, to join with other shareholders in tabling formal resolutions for discussion at a company's AGM. These are known as 'shareholder resolutions'. Shareholder resolutions are effective in showing investor concern on very specific issues. These prompt management to focus on those problems.

Legally, shareholder resolutions fall into different categories depending on where the company is based. The ease with which a shareholder can file also varies greatly. For companies listed in the UK, a shareholder must either hold 5% of the company's shares (out of reach for most investment houses) or club together with at least 100 other named shareholders with more than a minimal number of shares. That's also a difficult undertaking. Shareholder resolutions are much easier in the US, where all that is required is for two shareholders to work together, though the process is more heavily scrutinised by the regulator. Overall, we see far more shareholder resolutions in the US than in Europe. These often amount to several resolutions on a wide and varied set of topics at a single company.

Shareholder resolutions vary in their effect: some are binding but others are advisory. However, both kinds are vital tools in the kitbag of a responsible investor.

What happened in 2022

There is no restriction on which issues shareholders can raise through resolutions. However, the proposals must be sensible to make their way onto the ballot. For example, in English law, shareholder proposals must not be "frivolous or vexatious"[7]. In practice the easiest thing to do is to ask for a report on an issue - and that's what most resolutions request.

In 2022, we saw a large number of proposals covering racial equity - impartiality and fairness on race - in the US. Many gained strong support.

In the UK, a shareholder must either hold

5%

of the company's shares or club together with at least 100 other named shareholders.

On climate, resolutions usually ask companies to set more demanding emissions reduction targets. But we also saw efforts to quiz companies on whether their stated positions on climate change were consistent with their lobbying efforts.

7. Section 303(5)(c) of the Companies Act 2006

Shareholder proposals about civil rights gained strong support in the US

Company	Resolution	Result (Support)
The Home Depot	Racial Equity Audit	62.8%
Johnson & Johnson	Racial Equity Audit	62.6%
Altria Group	Civil Rights Audit	62.2%
McDonald's	Civil Rights Audit	55.1%
Waste Management	Civil Rights Audit	54.5%
Mondelez International	Racial Equity Audit	48.6%
Chevron	Racial Equity Audit	47.5%
American Water	Racial Justice Audit	47.1%
The Travelers Companies	Racial Justice Audit	46.6%
Charter Communications	Equal Employment Opportunities Data Disclosure	45.5%
Republic Services	Civil Rights Audit	38.4%
Republic Services	Environmental Justice Audit	35.3%

Source: Rathbones

Shareholders won majority backing for more than 40 ESG proposals in 2022

Environmental

Number voted: **30**
Number passed: **6**

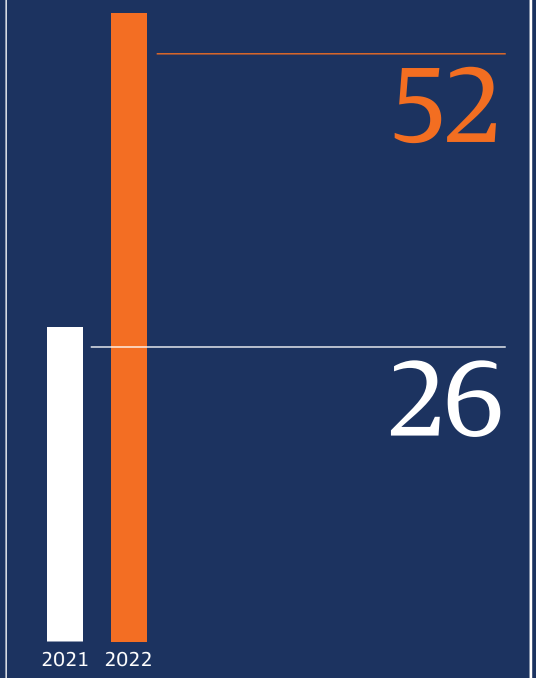
Social

Number voted: **107**
Number passed: **10**

Governance

Number voted: **149**
Number passed: **28**

The number of conservative shareholder proposals at US companies has doubled in a year



Source: Harvard Law School Forum on Corporate Governance. Data as of June 2022

There was also a rise in proposals by conservative shareholders at US companies. They included, for example, a proposal by the National Center for Public Policy Research for a racial equity audit at healthcare company Johnson & Johnson. This was motivated by a claim that employees deemed "non-diverse" could be discriminated against. Only 2.7% of Johnson & Johnson's shareholders voted in favour of this. However, along with 63% of shareholders, Rathbones voted for a more conventional racial equity audit.

What we did in 2022

We supported a record number of ESG shareholder proposals in 2022, covering the spectrum of E, S and G. The majority were filed at US companies. For instance, at Amazon we supported 12 shareholder proposals. These ranged from calling on the board to reduce plastic use to asking it to report on health and safety disparities between men and women and different ethnic groups. Rathbones generally supports proposals making reasonable requests for greater transparency on ESG matters. None of the resolutions gained majority backing. However, they received an encouraging level of support, showing the board that these remain key areas of concern for shareholders.

However, several shareholder proposals filed at large US companies and backed by us did gain majority backing. For instance, a proposal for The Home Depot to report on efforts to eliminate deforestation in its supply chain gained 65% support, while a climate proposal at ExxonMobil passed with 52% support. This asked the company to publish an audited report outlining how the International Energy Agency's modelling for a net zero global economy by 2050 would impact the "assumptions, costs, estimates, and valuations" underlying its financial statements.

To find out more about Rathbones' voting decisions, visit rathbones.com/investment-approach/responsible-investment

Important information

Rathbones

rathbones.com/responsible-investment

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Rathbones Group plc

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