2023 Proxy Season Review

Institutional Investor Expectations in a Divided World

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The 2023 proxy season reflected a post-pandemic "return to normal" with investors balancing increased focus on financial materiality with ESG considerations. Below are our top 11 takeaways from the 2023 proxy season.

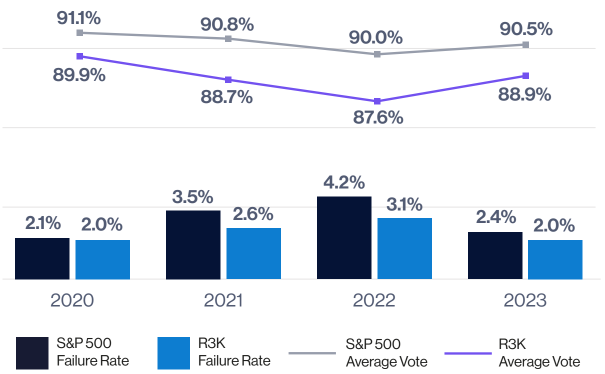
1. **Institutional investors go all-in on financial materiality.** Walking a thin line in a divided world of ESG, investors are choosing to pin their stewardship efforts around financial materiality and their fiduciary duty to act in their clients' best interests as long-term shareholders.
   - *As a result, ESG-related shareholder proposals that didn't align with investor views of materiality failed to generate significant investor support.*

2. **ESG focus weathers backlash, while greenwashing draws greater scrutiny.** Despite anti-ESG backlash, the term "ESG" is mentioned more frequently in 2023 sustainability reports than last year, as companies provided more detail about their ESG goals. Global institutional investors in the U.S. continue to integrate ESG as part of their investment process as described through their stewardship policies.
   - *Recently implemented regulations to combat greenwashing, such as the SEC's Names Rule, place pressure on investors to tie ESG-related voting decisions to investment objectives and portfolio performance.*

3. **Shareholders give thumbs up to lower CEO pay.** After years of rising pay levels and record low shareholder support, median CEO pay declined in 2022 by nearly nine percent.[1] Drivers of high pay such as incentive target adjustments and one-off awards were fewer as the impact of the pandemic subsided. As a result, vote support[2] for say-on-pay increased and failure rates dropped.

   - *The message from investors is clear: Aligning pay with performance is expected, but substantial pay increases and one-time awards may not be justified by performance alone.*

Figure 1: Say-on-Pay Vote Results



4. **Committee chairs face added pressures.** While average support for board candidates remained steady at 96 percent, more received below average support (<95 percent) in 2023 (26 percent) compared to 2022 (20 percent). The likely cause? Increasing investor pushback on committee chairs as they emphasize ESG accountability at the board and senior management levels through investment stewardship efforts.

   - *While the vote impact is minimal, new voting policies from investors and proxy advisors have created additional pressures for nominating and governance committee chairs, among others.*

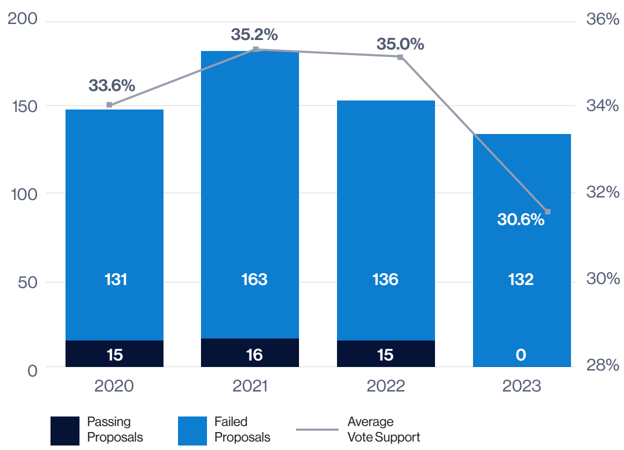
5. **The first year of universal proxy saw relatively few fights.** Despite early indications that 2023 could be the year of the large cap proxy fight, most fights failed to materialize. Instead, last proxy season was marked by settlements and litigation around the validity of dissident nominations. Among Russell 3000 companies, ten meetings went to a vote in the first half of 2023, compared to 11 in the first half of 2022.

   - *Activists will likely continue to target individual directors, so addressing potential concerns and filling skills gaps before an activist shows up should be a top priority for boards.*

6. **Shareholder proposals increased in quantity, but investors focused on quality.** Two years after the SEC amended the no-action request process, nearly 500 shareholder proposals made it to the ballot in 2023 and less than five percent passed. In contrast, only 331 proposals went to a vote in 2021, with a passing rate of over 18 percent. Environmental, social, governance and compensation proposals all saw lower proposal support and fewer passing votes. Many of the new proposals are much broader than in the past. The SEC is considering raising the bar for resubmitted proposals at previously targeted companies, potentially decreasing the number of proposals or causing proponents to seek new targets.

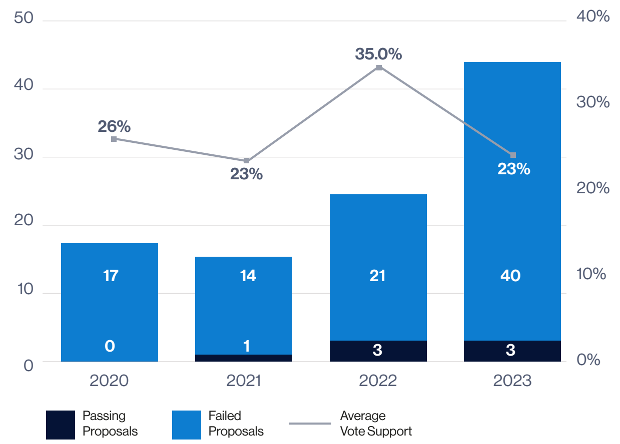
   - *Investors remain skeptical of proposals that are overly broad or prescriptive, particularly as they face pressure to link proxy votes to financial materiality.*

Figure 2: S&P 500 Governance Shareholder Proposals



1 Source: AFL-CIO Executive Pay Watch, October 10, 2023
2 Voting data reflects vote results from S&P 500 companies that held annual meetings between January 1, 2023 and June 30, 2023, compared to the same time period in prior years.

Figure 3: S&P 500 Compensation Shareholder Proposals



7. **Environmental proponents use shareholder proposals as a mechanism to deliver their message.** The voluntary withdrawal rate for environmental proposals fell from 26 percent in the 2022 proxy season to 16 percent in 2023. In many cases, proponents kept the proposals on the ballot despite low likelihood of investor support.

   - *Notwithstanding lower support for environmental proposals, shareholder proponents pushed harder to ensure their requests were presented and heard at the annual meeting.*

8. **Across social issues, proposals focused heavily on alignment between stated values and corporate action.** In 2023, over a quarter of social proposals requested companies to analyze their actions and impact for cohesion with corporate communications on topics such as workers' rights, political expenditures and racial equity.

   - *Proponents raise concerns about the reputational and business risks associated with misalignment as companies face pressure from internal and external stakeholders.*

9. **Lower support for broadly worded racial equity audit proposals reflects investor pragmatism.** Vote support for pro-ESG racial equity audits fell from 45 percent in 2022 to 21 percent in 2023. Rather than reflecting less shareholder interest in corporate diversity, it is likely that investors viewed these proposals as too broadly worded and expensive for the current economic outlook, especially at companies with robust DEI practices.

   - *As more companies publish the results of audits currently being conducted, pro-ESG proponents might alter their approach to these requests in future proxy seasons to be better tailored to individual company priorities.*

Figure 4: S&P 500 Environmental Shareholder Proposals

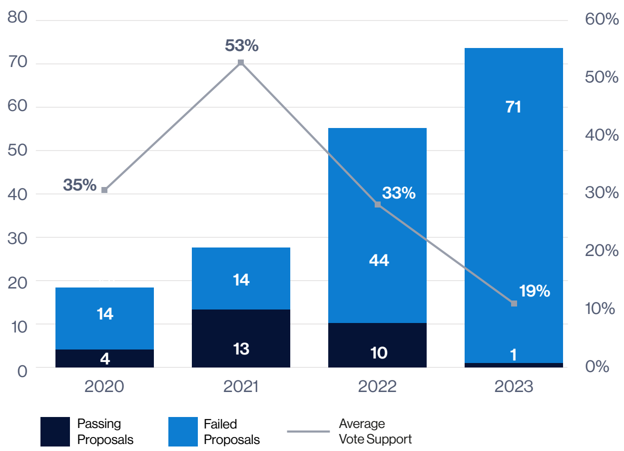
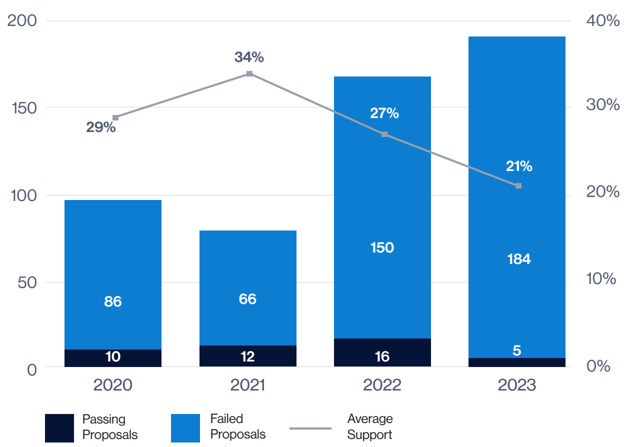


Figure 5: S&P 500 Social Shareholder Proposals

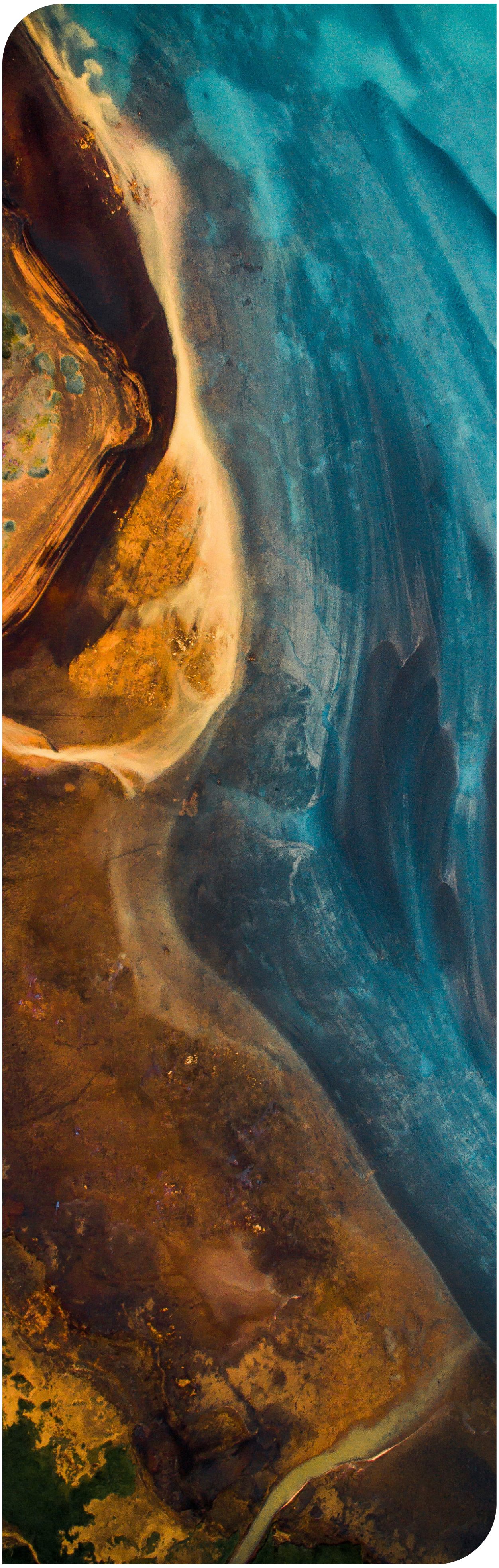


10. **Anti-ESG backlash failed to translate to support for anti-ESG proposals.** Investor support for anti-ESG proposals remained in the low single digits. Both institutional investors and issuers remain committed to ESG goals. However, the recent Supreme Court decision on affirmative action in college admissions is expected to energize the anti-ESG movement and potentially inspire an uptick in proposals alleging corporate DEI programs and practices as discriminatory.
    - *The current anti-ESG backlash is being driven by a loud minority rather than broad support.*

11. **The impact of pass-through voting is yet to be seen.** New pass-through voting policies at Blackrock and other large institutional asset managers have yet to significantly impact voting results, but the practice is still new and growing.
    - *The promise of more direct shareholder democracy must overcome the historically low participation rate from retail investors.*

Looking Ahead

The governance landscape continues to evolve as a raft of current and upcoming regulatory developments will impact the next proxy season. The SEC's recent cyber security rule and upcoming climate and human capital disclosure rules will give investors, including shareholder proponents, a wealth of new information to work with and critique. However, new disclosure requirements may render certain proposals on climate and workforce reporting obsolete. Threats of further congressional hearings and pressure from states' attorneys general continue to put ESG in the spotlight and force investors and issuers alike to defend their positions. The SEC's potential changes to shareholder proposal resubmission requirements (rule 14a-8) may raise the bar for proponents to resubmit their proposals at previously targeted companies. Furthermore, new and emerging issues demand attention as various strikes elevate workers' rights issues and investors solidify policies on the responsible use and oversight of AI. As the landscape becomes increasingly complex, issuers must prepare strategically to meet the evolving needs of stakeholders.



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