Environmental and social concerns dominate the 2019 proxy season

Environmental and social (E&S) proposals composed the majority of shareholder proposals filed this proxy season, a trend that continues for the third year in a row. However, nearly half of the 438 E&S proposals filed were withdrawn, according to ISS Analytics, which signifies companies are "doing a good job of reaching out to shareholders" and negotiating, according to Pamela Marcogliese, reflecting on the 2019 proxy season during the June 2019 KPMG Quarterly Webcast.

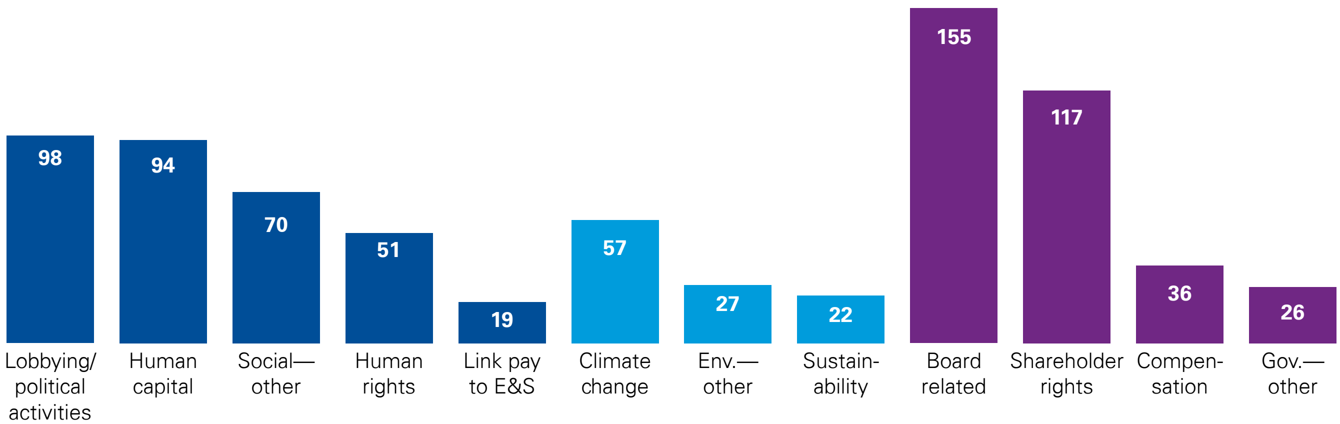
"Companies are increasingly better at presenting their views on some of the environmental, social, and governance (ESG) issues and have been spending a lot more time on these issues throughout the year. And shareholders are more proficient and have organized well," said Marcogliese, a partner at Cleary Gottlieb Steen & Hamilton in New York who advises companies on proxy disclosures, shareholder engagement, and other governance matters. "There has been better disclosure and better engagement on the company side and more organization on the shareholder proponent side. Both sides have really been stepping up their game," said Marcogliese.

Joined by Stephen Brown, Senior Advisor, KPMG Board Leadership Center, Marcogliese reviewed recent proxy voting results and shared her views on E&S shareholder proposals, human capital management (HCM) considerations, board composition, and the outlook for next year's proxy season.

Figure 1

Total E&S proposals outnumber governance proposals in early 2019

number of shareholder proposal filings by proposal category (as of June 1, 2019)



Source: ISS Analytics as of June 1, 2019.

Social (332) Environmental (106) Governance/Compensation (334)

E&S shareholder proposals

"E&S-type issues are just now beginning to enter mainstream consciousness, while people have been focusing on the 'G' in ESG for a very long time," said Marcogliese, explaining the relative growth in E&S-focused proposals compared to traditional governance proposals (See Figure 1, p. 1).

Although many of this year's E&S proposals were withdrawn before going to a vote, there has been increased shareholder support for E&S proposals and "we have to be mindful of the impact of the government shutdown," Marcogliese said. "We saw an even greater increase in engagement, with companies trying to figure out whether there was a negotiated path forward as a way to backstop the possibility that they wouldn't get no-action relief in time."

The upcoming presidential election was also largely responsible for the nearly one quarter of E&S-related proposals calling for disclosure of lobbying and related political activity.

In light of the increased shareholder focus on ESG, only 25 percent of participants who responded to a poll during the webcast expressed confidence that their companies were effectively managing critical ESG issues (Figure 2).

Marcogliese encouraged directors and senior management to consider the intentions of shareholder proposals in the context of the company's overall strategy: "There's a difference between caring about [E&S] issues and thinking that a proposal is the right strategy for a company. Reaching out to shareholders, understanding what their individual issues are, and explaining to them what the company is doing is really the path forward," she said.

HCM considerations

Shareholders, employees, and other stakeholders are demonstrating higher expectations for companies and their directors to make progress on HCM issues, such as gender and racial/ethnic diversity, pay equality, employee retention, and corporate culture, among other areas. A 2019 survey by Morrow Sodali indicates that 83 percent of global investors support greater disclosure around HCM.[1]

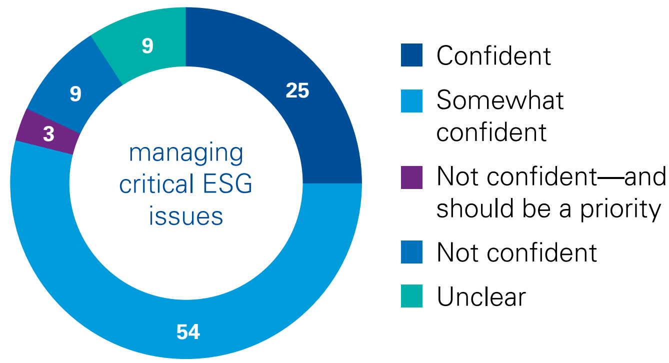
"Many large investors focus on human capital whenever they put out their annual letters to companies or CEOs," said Marcogliese. "In his letter this year, [BlackRock CEO] Larry Fink had a focus on [the company's responsibility in regards to] retirement and making sure that employees have the wherewithal to retire adequately."

Figure 2

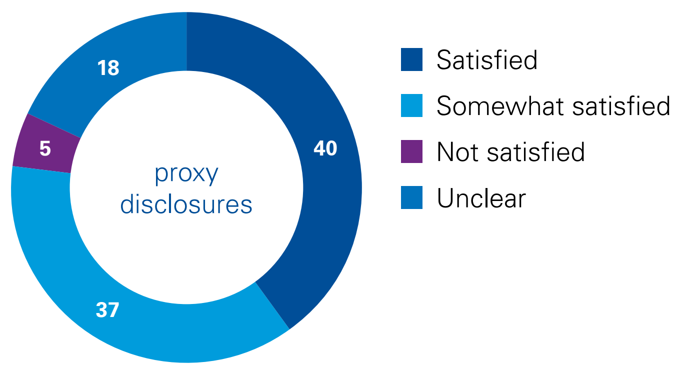
KPMG Quarterly Webcast survey results

values shown in percentages

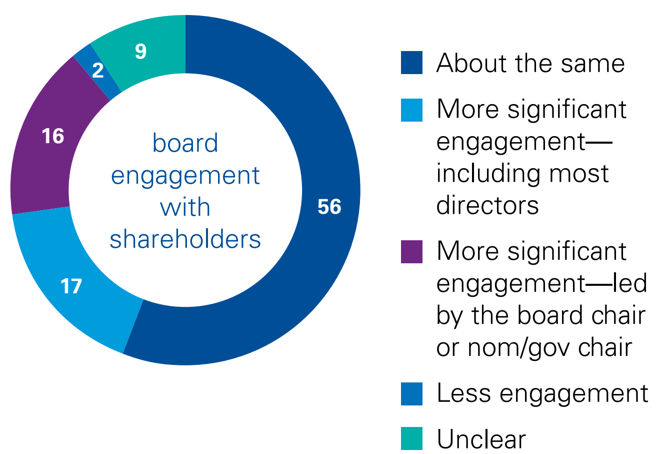
How confident are you that your company is aware of, and effectively managing, the critical ESG issues—e.g., environment and climate, health and safety, human rights, data privacy, diversity and corporate culture—that pose a material risk to the company's performance and reputation?



How satisfied are you that your company's proxy disclosures address key areas of interest to investors, such as strategy, culture, ESG, and board composition and diversity?



How has your board's engagement with shareholders changed over the past two to three years?



Of 305 self-identified corporate directors, senior executives, and senior legal advisors on the June 20, 2019, KPMG Quarterly Audit Committee Webcast.

[1] Cleary Gottlieb Steen & Hamilton LLP, "2019 Post-Proxy Season Review and Governance Trends," June 2019.

Marcogliese also highlighted the rise in shareholder activism by employees with significant stock ownership who are frustrated about an issue. "It's creating an interesting dynamic," she said. "You may have thought that shareholder proposals are limited to proxy season, but that's not the case when your employees are the shareholder proponents. The employee/shareholders show up to work [after the annual meeting] and continue the conversation."

Board composition

"Board refreshment is one of the top topics in boardrooms today," said Marcogliese. According to the *2018 Spencer Stuart Board Index*, 33 percent of new S&P 500 corporate directors were first-time directors and only 36 percent had C-suite experience (Figure 3). Additionally, 45 percent of new Russell 3000 board seats in 2018 were filled by women and 15 percent by ethnic minorities. "Investors are very focused on where women sit once they are on the board. What committees are they on? Are they chairs?"

Figure 3
S&P 500 board composition in 2018

428	new independent directors were elected, the highest number since 2004.
63	was the average age of independent directors, up two years since 2008.
40%	of new directors were women, with women representing 24% of all directors.
36%	of new directors had C-suite experience, a drop from 47% in 2008.
33%	of new directors were first-time directors, up from 24% in 2008.
17%	of directors in the top 200 S&P 500 companies were minorities, only a slight increase from 14% in 2008.

Source: *2018 Spencer Stuart Board Index*

The conversation regarding board tenure "is a lot more thoughtful," said Marcogliese, with investors looking more at the mix of tenures on the board and the benefit of having directors across the tenure spectrum. Additionally, investors are placing greater focus on diversity in senior management. "What does the C-suite look like and what does the pipeline look like? What are your training programs and development and retention goals?" asked Marcogliese. "There is significant focus from an engagement perspective in trying to understand what is going on."

Figure 4
Sample overboarding policies
These large institutional investors and proxy advisory firms have overboarding policies in place that may result in votes against/withheld votes from the following directors:

	Vanguard	BlackRock	State Street	Glass Lewis	ISS
Inside Directors	Named executive officers (NEOs) who sit on more than 2 public company boards (except at the company where the director is an NEO)	CEOs who sit on more than 2 public company boards	CEOs who sit on more than 3 public company boards	NEOs who sit on more than 2 public company boards (except at the company where the director is an NEO)	CEOs who sit on more than 3 public company boards (except at the company where the director is an CEO)
Outside Directors	All other directors who sit on more than 4 public company boards (except generally where the director is the chair)	All other directors who sit on more than 4 public company boards	All other directors who sit on more than 6 public company boards	All other directors who sit on more than 5 public company boards	All other directors who sit on more than 5 public company boards

Source: Cleary Gottlieb Steen & Hamilton

Marcogliese also commented that directors need to be mindful of overboarding policies announced by institutional investors (Figure 4). "Unless companies and directors manage these numbers, we're going to start seeing approval rates for director re-elections come down over the next couple of years."

"Off cycle" engagements

According to Marcogliese, it has become standard practice for companies to engage with their top investors outside of proxy season to discuss the company's long-term strategy and targets and to help build a firmer foundation for support. A clear agenda and preparation are key to successful shareholder engagements.

Outlook for the 2020 proxy season

"The 2019 proxy season is best characterized, relatively, by the absence of major surprises or new themes that we hadn't seen before," said Marcogliese. "I think that 2020 will likely be a continuation of 2019, with better disclosure and engagement from companies and better organization from shareholders."

For the full replay and other highlights, visit kpmg.com/us/aciwebcast.

About the KPMG Board Leadership Center

The KPMG Board Leadership Center champions outstanding governance to help drive long-term corporate value and enhance investor confidence. Through an array of programs and perspectives—including KPMG's Audit Committee Institute, the WomenCorporateDirectors Foundation, and more—the Center engages with directors and business leaders to help articulate their challenges and promote continuous improvement of public- and private-company governance. Drawing on insights from KPMG professionals and governance experts worldwide, the Center delivers practical thought leadership—on risk and strategy, talent and technology, globalization and compliance, financial reporting and audit quality, and more—all through a board lens. Learn more at kpmg.com/us/blc.

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