



ESG Voting Policy Overlay

2022 Year End Report

The ESG Voting Policy Overlay complements investors' traditional corporate governance polices to align voting activities with ESG issues most important to investors.

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This report summarizes the ESG Voting Policy Overlay recommendations, and more generally, insights from the 2022 Proxy Voting season.

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Why Governance Matters

The core pillars of good governance are fundamental to sustainable business: board independence, transparency, measurable performance metrics, engaging with external stakeholders, internal controls as well as reporting that ensures boards stay informed and senior management remains answerable. Collectively, these arrangements are often referred to as the 'G' in ESG. But it's time to take a closer look at how governance serves the modern view of business.

Many of the dominant corporate governance practices today best serve the now-outdated shareholder primacy corporate governance paradigm. For example, the over-use of stock-based awards and share price performance measures for paying senior executives; drawing exclusively from a narrow pool of retired CEOs and senior executives for board succession; limiting board-level external interactions to only the largest shareholders. These practices undermine the pursuit of long-term shared value for all stakeholders.

The stakeholder paradigm expects companies to pursue a broader purpose than profit maximization and to take into account societal impacts across their value chain. This is the view that is increasingly embraced by investors, regulators, and forward-thinking business leaders.

The paradigm shift was already happening well before the COVID pandemic – fueled by a post-financial crisis awakening to the systemic vulnerabilities introduced by short-termism, as well as a growing urgency for global action to halt climate change. However, 2020 brought to the fore fundamental flaws in shareholder primacy-style governance. The economic and political fallout ignited a collective awareness of the overlapping interests of stakeholder groups in securing resilience across systems. As we explore in Section 4, boards and pay practices are adjusting, but not quickly enough.

Section 1 of this report summarises the ESG Voting Policy Overlay's 2022 voting recommendations. In Section 2 we spotlight the 2022 Japanese proxy season. Section 3 gives a roundup of some of the key regulatory developments shaping corporate governance, sustainability reporting and shareholder voting rights in 2022. Section 4 takes a critical look at current board-level ESG credentials and senior executive pay practices and puts forward priorities for 2023. Section 5 reviews investor biodiversity initiatives to further the goals of the Global Biodiversity Framework that emerged from COP 15. Section 6 summarises two areas in which we've enhanced our voting approach going into 2023.

Key Takeaways

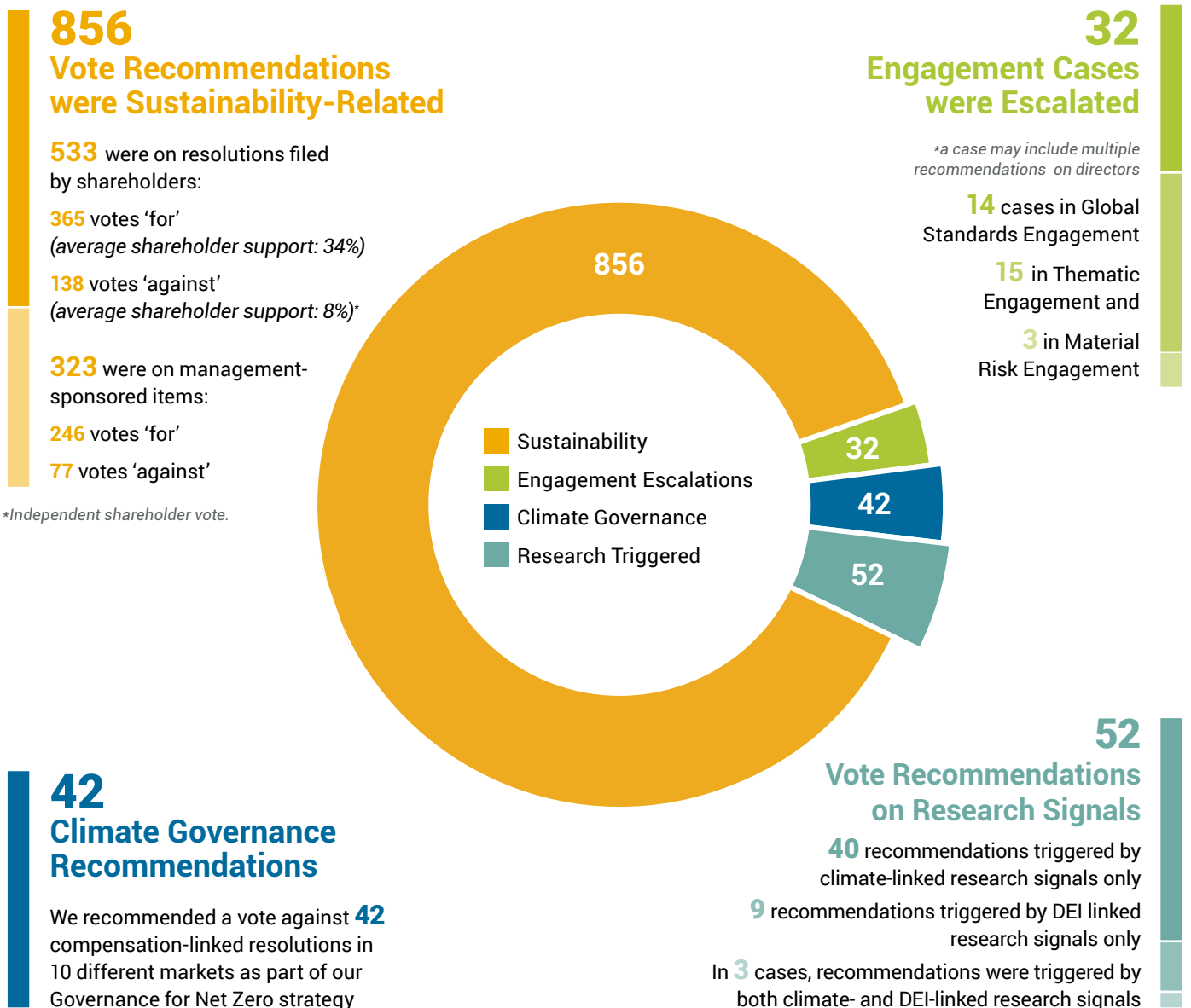
1. Board members' views about their responsibility for oversight of ESG are often out of step with investor expectations, according to recent board and investor surveys. Stronger board diversity standards can bring new skills and backgrounds into the corporate director pool.
2. As inflation erodes workers' real wages, 2023 could see heightened scrutiny of C-suite pay practices and a possible backlash on pay-related proxy votes. Investors are asking boards to show restraint in deciding performance outcomes with the potential for windfall payouts, and to link pay to sustainability.
3. Governments and standards setting agencies accelerated the pace of rule making in 2022, with a series of new or proposed measures advancing sustainability reporting, board diversity, and shareholders' voting rights.
4. Shareholder advocacy is on the rise. In the brief and packed 2022 Japanese proxy season, asset managers joined with civil society groups to file more ESG shareholder resolutions, earning higher support for climate measures.
5. The successful conclusion of COP15 saw the ratification of a new framework tackling biodiversity loss. Investor biodiversity initiatives are applying the climate action playbook to push companies for targets, actions and nature-related reporting.



1. Our Votes in 2022

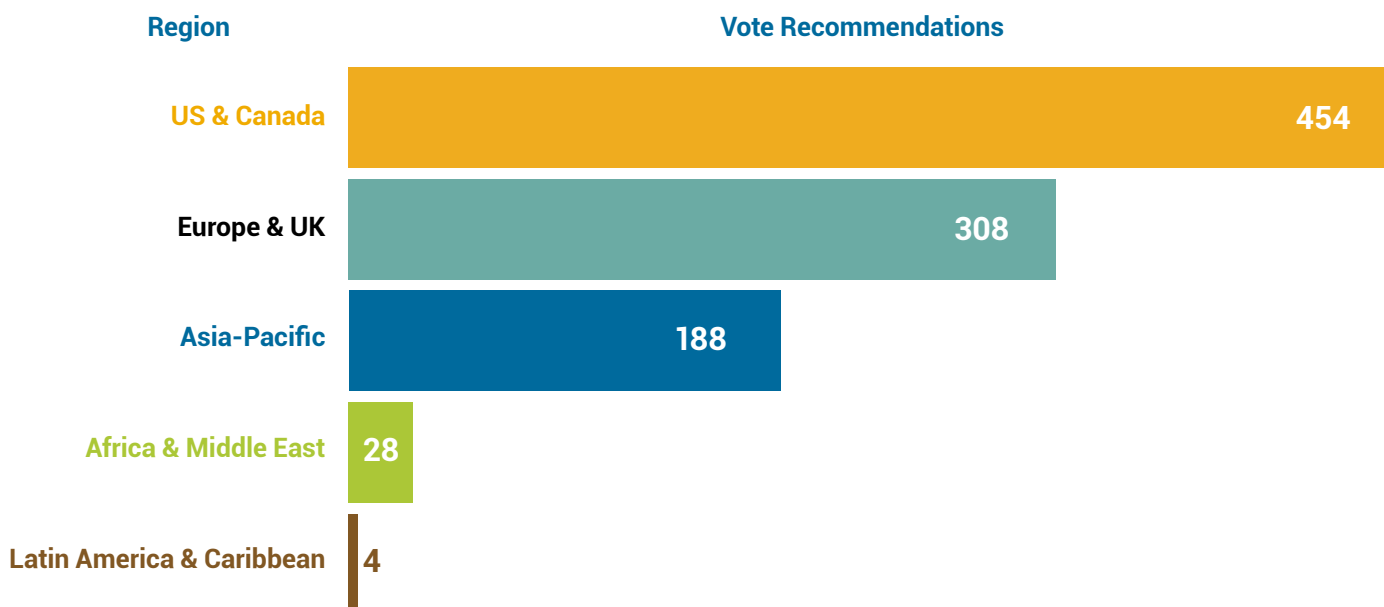
In 2022 we developed **982** voting recommendations with supporting research across **628** meetings held by companies in **33** markets and **44** industries. Of these, **856** recommendations applied to **sustainability-focused ballot items**, with **533** recommendations on shareholder resolutions and **323** recommendations on resolutions proposed by corporate management. **Thirty-seven** management-sponsored resolutions requested approval of companies' **climate transition plans** – also known as '**say-on-climate**', on which we recommended a vote 'Against' in **10** cases. In **52** cases we recommended a vote against certain board members or against the approval of the company's accounts based on Sustainalytics' ESG research showing poor management of **climate** or **diversity**. In **32** cases, we supported the **engagement team to escalate a vote against management** where companies failed to engage meaningfully on ESG topics of relevance to investors. For our **Governance for Net Zero** voting strategy, we examined pay arrangements of **70** large fossil fuel companies and in **42** cases recommended a vote against the company's say-on-pay resolution (or another compensation-linked resolution) where Scope 3 targets were missing from incentive pay.

We delivered **982** Vote Recommendations across **33** Markets and **44** Industries





By far the largest number of vote recommendations applied to North American companies, with 36 AGMs held by Canadian companies and 180 by US companies. Across the 308 recommendations in Europe and the UK, we offered recommendations on 208 political donations resolutions at UK company AGMs. Of the 188 vote recommendations at Asia-Pacific company meetings, 43 applied to 18 Australian company meetings and 86 applied to 23 Japanese company meetings, with the remainder voted across 58 meetings in 8 other markets comprising the Asia-Pacific region.



2. Spotlight on the Japanese Proxy Season

Japan is a unique market. Its concentrated proxy season – with hundreds of general meetings taking place around a three-day period at the end of June each year – marks a blistering end to the shareholder voting season. It has long been considered a laggard among developed markets when it comes to ESG practices. Whether it be management-dominated boards, a lack of diversity, the prevalence of cross-shareholdings, poor disclosures, or non-responsiveness to shareholder engagements, Japanese company practices have been slower than other developed markets in adapting to the changing ESG landscape.

However, recent regulatory developments and ongoing efforts from investors are moving the dial on issues like gender diversity and climate-change.

Shining a Light on the Gender Gap

A mandatory wage gap disclosure rule under Prime Minister Kishida’s “New Capitalism” policy¹ aims to require companies with more than 300 employees to disclose their gender pay gap data, and the ratio of women in management positions from fiscal year 2023 onward. With the third largest wage gap out of OECD countries,² shining a spotlight on this issue can only help to ensure that Japanese workforces and boardrooms are reflective of the country’s wider population and its diverse viewpoints.

Mandatory Climate Reporting

Greater attention is being paid to sustainability at Japanese companies. In 2021, amendments to the Japanese Corporate Governance Code³ were aimed at increasing corporate value by requiring companies to develop policies and initiatives on sustainability. This required Prime Market-listed companies to:

1. Provide climate disclosures based on the Task Force on Climate-related Financial Disclosures (TCFD) or equivalent international frameworks, and
2. Set policies and goals for promoting gender diversity and diversity based on nationality.

In addition, the code requires that companies now publish their reports in English, making it easier for international investors and the general public to evaluate climate reports.

1. The Government of Japan (2022). PM Kishida’s Speech on the New Form of Capitalism and Why Japan Is a “Buy”, accessed (24.01.23). https://www.japan.go.jp/kizuna/2022/06/why_japan_is_a_buy.html.
2. OECD (2022). Gender wage gap, accessed (24.01.23). <https://data.oecd.org/earnwage/gender-wage-gap.htm>.
3. Tokyo Stock Exchange (2021). Japan’s Corporate Governance Code, accessed (24.01.23). <https://www.jpx.co.jp/english/news/1020/b5b4pj0000046kxj-att/b5b4pj0000046l0c.pdf>





Shareholder Advocacy

The greater focus on sustainability in Japan is also reflected in shareholder resolutions tabled at Japanese company AGMs in recent years. With the effects of the 2011 Fukushima disaster still fresh in the minds of so many, Japan's power companies typically face multiple resolutions calling for them to exit nuclear power or adopt additional safety measures.

However, civil society organizations, such as Market Forces, 350.org Japan, Friends of the Earth Japan, Kiko Network and Rainforest Action Network, have brought several climate-related resolutions in recent proxy seasons, including at least six in 2022 filed at Mitsubishi Corp, Chubu Electric, Tokyo Electric and Sumitomo Mitsui Financial Group.

In Japan, shareholder proposal filers must own at least 1% or 300 voting rights for the preceding 6 months. Reaching one of these thresholds may require some coordination of interested investors.

The Australasian Centre for Corporate Responsibility, or ACCR, co-ordinated a joint filing of a set of three climate resolutions at Electric Power Development Co, or J-Power, on behalf of European institutional investors, HSBC Asset Management, Amundi, and Man Group.⁴ According to the filers, J-Power is Japan's largest coal power operator. The proposals ask the company to set and disclose credible emissions reduction targets and align capital expenditure and senior executive remuneration with these targets.

Since, under Japanese law, shareholder proposals on climate change would typically be framed as amendments to the company's articles of incorporation, support levels, where reported, remain relatively low. However, with a growing international investor base, some resolutions received levels of support not previously attained for Japanese companies. At Sumitomo Mitsui Financial Group, for instance, support reached 27% on a climate resolution, where a similar proposal voted in 2021 received 20%.

We anticipate that shareholder groups will maintain their pressure on Japanese companies in 2023, focusing in particular on climate targets at the countries' heaviest emitters and at their financiers.

4. Australasian Centre for Corporate Responsibility (2022). Strong call by J-Power shareholders to strengthen decarbonisation strategy, accessed (24.01.23). <https://www.accr.org.au/news/strong-call-by-j-power-shareholders-to-strengthen-decarbonisation-strategy/>

Table 1: Climate Resolutions Voted at Japanese Companies in 2022

Company	Title	Management's Vote Recommendation	Sustainalytics' Vote Recommendation	Reported Support	Independent Shareholder Support
Chubu Electric Power Co.	Report on Resilience of Assets	Against	For	19.9%	19.9%
Electric Power Development Co. (J-Power)	Link Executive Compensation to GHG Targets	Against	For	18.9%	18.9%
Electric Power Development Co. (J-Power)	Align Business Strategy to the Paris Agreement	Against	For	25.8%	25.8%
Electric Power Development Co. (J-Power)	Align Capex with GHG Targets	Against	For	18.1%	18.1%
Kansai Electric Power Co.	Conduct and Report on Scenario Analysis up to 2050	Against	For	*	*
Kansai Electric Power Co.	Link Executive Compensation to ESG Targets	Against	For	*	*
Kansai Electric Power Co.	Prohibit New Coal Fired Power Generation	Against	For	*	*
Kansai Electric Power Co.	Withdraw from Coal-Fired Thermal Power Generation	Against	For	*	*
Mitsubishi Corp.	Align Business Strategy to the Paris Agreement	Against	For	20.2%	20.2%
Mitsubishi Corp.	Align CapEx with Net Zero by 2050 Scenario	Against	For	16.2%	16.2%
Tokyo Electric Power Company Holdings	Report on Resilience of Assets	Against	For	9.6%	20.0% ¹
SK Kaken Co.	Disclose Greenhouse Gas Emissions	Against	For	*	*
Sumitomo Mitsui Financial Group	Align Business Strategy to the Paris Agreement	Against	For	27.0%	27.0%
Sumitomo Mitsui Financial Group	Align Fossil Fuel Financing with IEA's Net Zero Scenario	Against	For	10.0%	10.0%

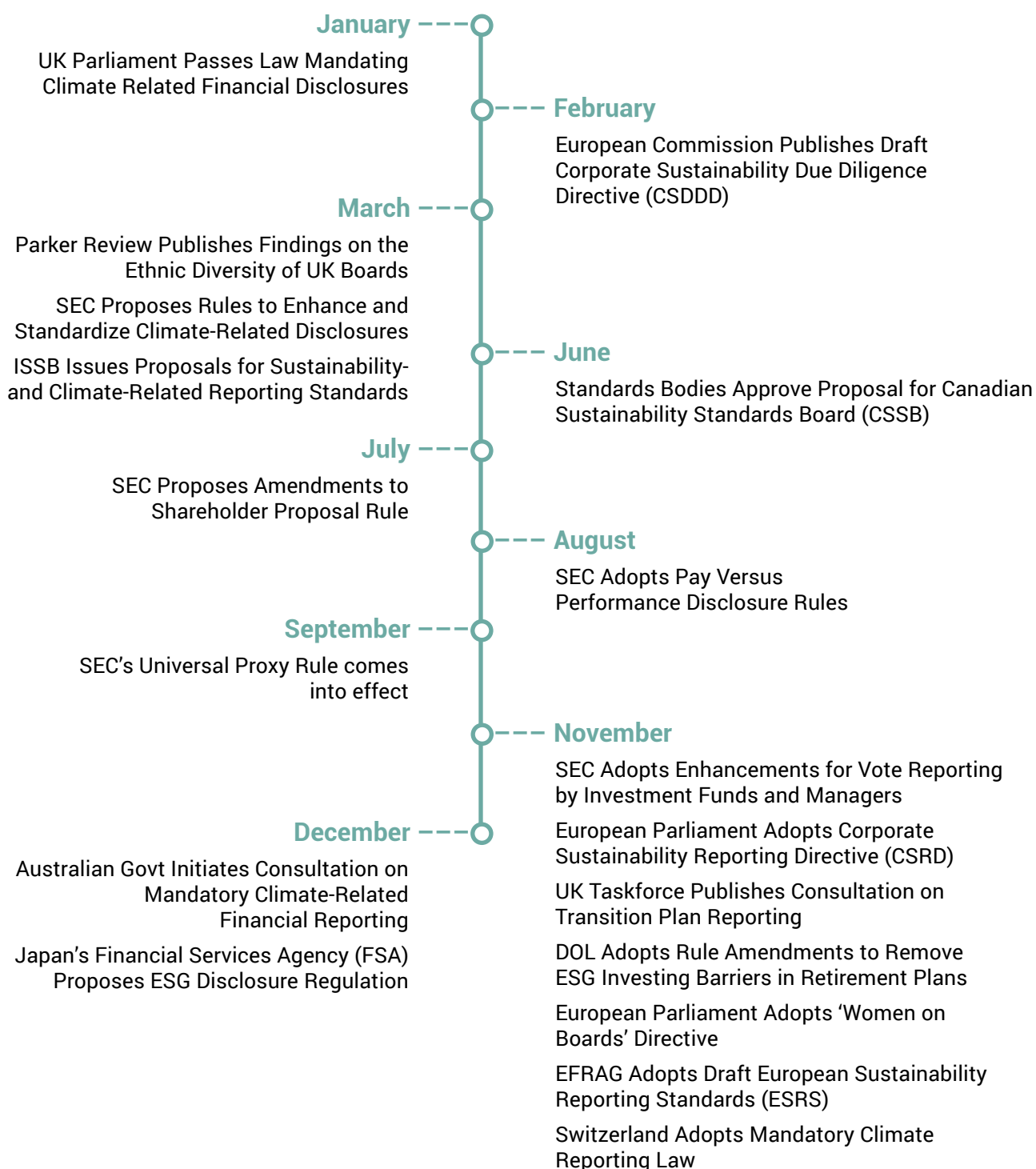
* Not Reported

1. Excluding Government Shareholding

3. Corporate Governance Roundup: Regulatory Developments Across Markets

Governments, regulators, and standards-setting agencies accelerated the pace of rule making in 2022, with a series of new and proposed measures advancing sustainability reporting, board diversity, as well as shareholders' voting rights. Appendix 1 contains a brief description of each of the important regulatory developments.

2022 Regulatory Developments



4. Calibrating Corporate Governance for a New Paradigm

4.1 Are Boards Ready for ESG in 2023?

The board's role is to create long-term value by setting the purpose and strategic direction of the company and overseeing the implementation of a corporate strategy that delivers sustainable returns.

Board Member Views Out of Step with Investor Expectations

PwC's 2021 Global Investor Survey finds that ESG is an important factor in investment decision making for 79% of investors and that 82% of investors believe that companies should embed ESG directly into their corporate strategy.⁵ This means that investors expect boards to be fluent in social, environmental, and governance business factors, as well as driving the integration of ESG into their corporate strategy.

However, only 57% of US public company directors say ESG issues are linked to company strategy and only 55% of directors report that ESG was regularly part of the board's agenda in the preceding year, according to PwC's 2022 Annual Corporate Directors Survey. Fewer still believe that ESG issues actually have an impact on company performance (45%), and only 13% think that reputational risks are a significant challenge for boards to oversee. Most concerningly, a mere 11% of directors believe that environmental/sustainability expertise is important for their board.⁶

In Europe, 82% of directors and senior management report that ESG is discussed frequently or at every board meeting, yet 43% of senior management and directors believe that boards lack sufficient commitment to integrate ESG factors into corporate strategy, according to a 2022 EY board survey.⁷

Outdated views may be holding boards back from embracing ESG; in particular, the belief that generating near-term financial returns for shareholders takes primacy over other stakeholder interests. A lot of boards may struggle with how to prioritize ESG, which typically requires a longer-term strategic horizon.

5. PwC (2021). PwC's 2021 Global Investor Survey, accessed (24.01.23).

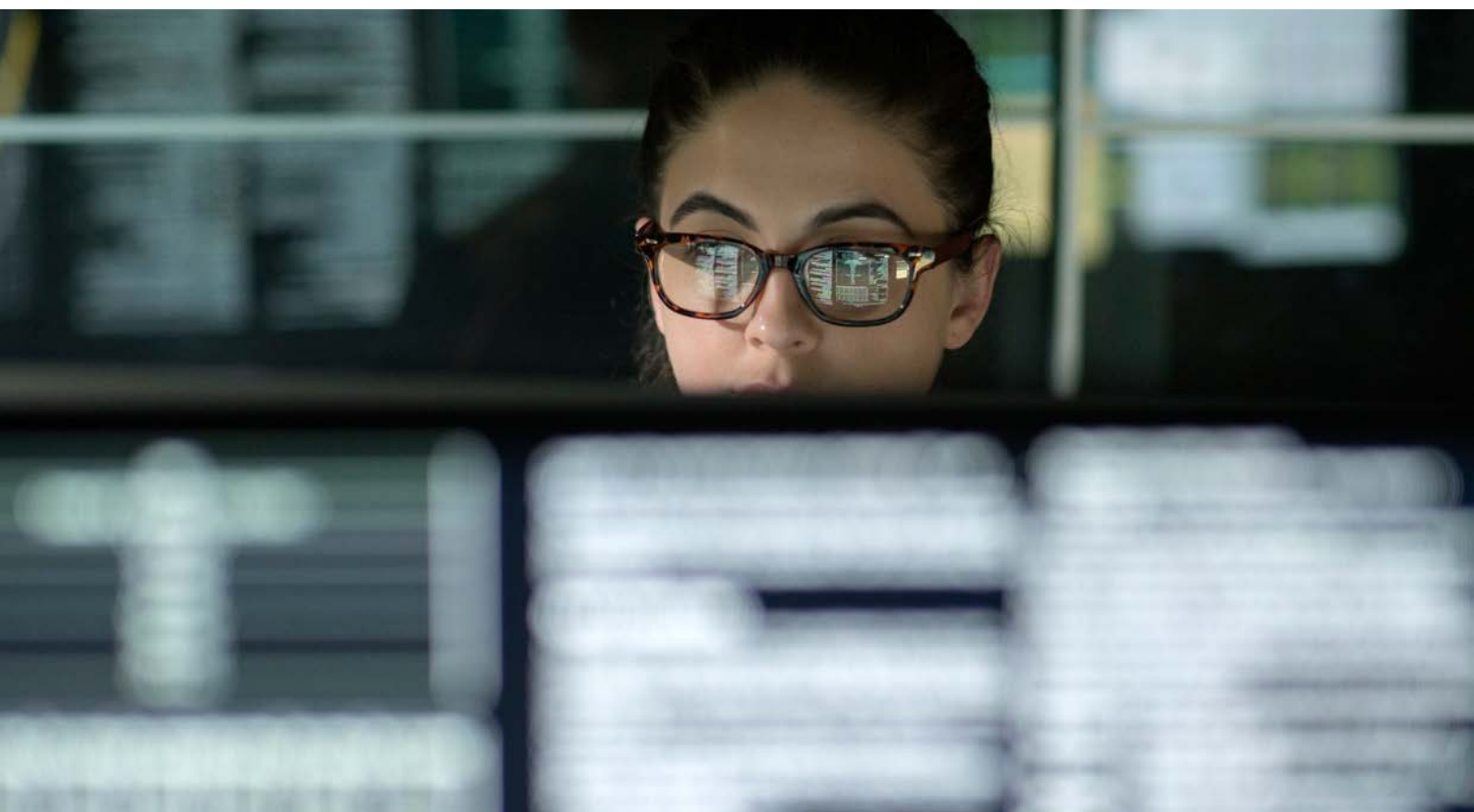
<https://www.pwc.com/gx/en/services/audit-assurance/corporate-reporting/2021-esg-investor-survey.html>

6. PwC (2022). 2022 Annual Corporate Directors Survey, accessed (24.01.23).

<https://www.pwc.com/us/en/services/governance-insights-center/library/annual-corporate-directors-survey.html>

7. EY (2022). How can boards strengthen governance to accelerate their ESG journeys? EY Long-Term Value and Corporate Governance Survey, accessed (24.01.23).

https://assets.ey.com/content/dam/ey-sites/ey-com/en_gl/topics/attractiveness/ey-long-term-value-and-corporate-governance-survey-february-2022.pdf





Diversity, Board Renewal and Good Governance

Board ‘myopia’ is regularly linked to a lack of board diversity.⁸ There is broad consensus among investors that board diversity is a basic tenet of good governance, and a growing number of markets require boards to work towards time-bound diversity targets.

Diversity considerations focus attention on the collective competencies and qualities of a board – a calculus that incorporates personal characteristics and backgrounds such as gender, nationality, ethnicity, gender identity, as well as the skills, expertise, perspectives, and independence of the board as a whole.

Consider how this can impact climate governance. Whereas 66% of female directors agree with prioritizing climate action, even if it impacts short-term performance of the company, only 45% of male directors endorsed this position in PwC’s board member survey.⁹ Furthermore, understanding climate transition plans and climate litigation risks may require expertise in emerging disciplines not readily available from within the pool of serving or retired C-suite executives.¹⁰

In addition, 86% of board members agree that diversity enhances the board. Yet 34% believe that new candidates are not needed and 31% believe that new candidates are not qualified.¹¹

Investor and regulatory pressure for greater board diversity is challenging boards and their service providers to take new approaches to board renewal, with the goal of cultivating a forward-looking mindset and stronger ESG competencies.

Engagement Can Help Boards

ESG is driving engagements and more boards are engaging directly with investors to understand how best to orient governance practices to address ESG challenges. What’s more, 61% percent of investors that adopt ESG investment strategies indicate that ESG is a topic of engagement with corporate boards of investee companies.¹² In 2022, 60% of directors say that a member of their board (other than the CEO) engaged directly with shareholders within the previous 12 months, up from 42% in 2017.¹³

Through engagement, boards can gain insights into leading governance practices, reflect on their own governance weaknesses, communicate timelines for implementing governance improvements, and avoid embarrassing ballot results. For many investors, board responsiveness to engagement is itself a good governance practice.

While board diversity has become a routine consideration in director elections, more large institutions are explicitly incorporating additional ESG expectations into their votes on directors.

8. Eccles, R.G.; Johnstone-Louis, M.; Meyer, C.; Stroehle, J.C. (2020). The Board’s Role in Sustainability. Harvard Business Review (September-October), accessed (24.01.23). <https://hbr.org/2020/09/the-boards-role-in-sustainability>

9. PwC, 2022 Corporate Director Survey, accessed (24.01.23).

10. Climate Governance Initiative (2022). COP27: Key outcomes for board directors, accessed (24.01.23).

<https://climate-governance.org/cop27-key-outcomes-for-board-directors/>

11. PwC, 2022 Corporate Director Survey.

12. BNP Paribas (2022) The ESG Global Survey 2021, accessed (24.01.23). <https://www.theia.org/sites/default/files/2021-09/The%20ESG%20Global%20Survey%202021.pdf>

13. PwC, 2022 Corporate Director Survey.

4.2 Looming Backlash Against Executive Pay in 2023?

Going into the 2023 proxy season, boards should prepare for heightened scrutiny of senior executive pay practices. As investors weigh their 2023 say on pay votes, questions of fairness and links to ESG are likely to be key considerations.

The Growing Worker-CEO Pay Gap is a Problem

CEOs took home bumper pay packages in 2021. In the US, pay awarded to S&P 500 company CEOs jumped 19%, having increased by 7% in 2020. In the UK and Canada, where large companies' CEO pay dipped in 2020, pay jumped by 23% in 2021.¹⁴

By contrast, workers' real wages fell in the first half of 2022 across G20 countries.¹⁵ For the lowest income-earners, the cost-of-living impacts weigh far heavier – driving societal inequality and risking social unrest and political instability.

CEO to typical worker pay ratios track diverging fortunes. Top CEOs in the UK earned 109 times that of median employees in 2021.¹⁶ In Canada the multiple was 243 against average worker salary.¹⁷ In the US, S&P 500 CEO to median worker pay stood at around 320, according to Morningstar's Executive Insight data.

Last year, 87% of Americans viewed the growing worker-CEO pay gap as a problem.¹⁸ In the UK, widespread strike action has been linked to a growing sense of unfairness experienced by workers struggling under the cost-of-living crisis.¹⁹

Investor opinion may also be turning. Governance professionals report a large increase in the frequency of investor questions on executive compensation plans over the past two years.²⁰

Say on Pay Gives Shareholders a Voice on Pay Practices

Shareholder approval of senior executive pay practices, also called 'say-on-pay', is a standard ballot measure in many jurisdictions. It is required in the UK, US, EU, Australia, South Africa and adopted as general practice by most large companies in Canada.

Average support for say on pay at the largest US companies has been inching down over the past five proxy seasons, sinking from a high of 92.1% in 2014 to 87.7% in 2021. Nearly five percent failed to earn majority support in 2022. This trend should concern boards.

14. PwC (2022). Executive pay at FTSE 100 firms recovers to pre-pandemic levels, accessed (24.01.23).

<https://www.pwc.co.uk/press-room/press-releases/executive-pay-at-ftse-100-firms-recovers-to-pre-pandemic-levels.html> and Milstead, D. (2022). CEOs at Canada's largest companies saw 23-per-cent pay increase in 2021. The Globe and Mail, 4 July 2022, accessed (24.01.23).

<https://www.theglobeandmail.com/business/article-ceos-at-canadas-largest-companies-saw-23-per-cent-pay-increase-in-2021/>

15. International Labour Organization (2022). Rising inflation brings striking fall in real wages, accessed (24.01.23).

https://www.ilo.org/global/about-the-ilo/newsroom/news/WCMS_862321/lang-en/index.htm

16. PwC (2022). Executive pay at FTSE 100 firms.

17. McDonald, D. (2023). Breakfast of Champions CEO pay in 2021 hits new all-time high. Canadian Centre for Policy Alternatives, 3 January 2023, accessed (24.01.23). <https://policyalternatives.ca/publications/reports/breakfast-champions>

18. Just Capital (2022). Americans Say CEO Pay Is Too High: Companies Should Reduce Income Inequality by Raising Minimum Wage to Living Wage and Capping CEO Compensation, accessed (24.01.23). <https://justcapital.com/reports/survey-analysis-americans-say-ceo-pay-is-too-high-companies-should-reduce-income-inequality-by-raising-minimum-wage-to-living-wage-and-capping-ceo-compensation/>

19. Young, S. (2022). Strikes: why soaring CEO pay could help explain UK's recent industrial action. The Conversation, November 2022, accessed (24.01.23).

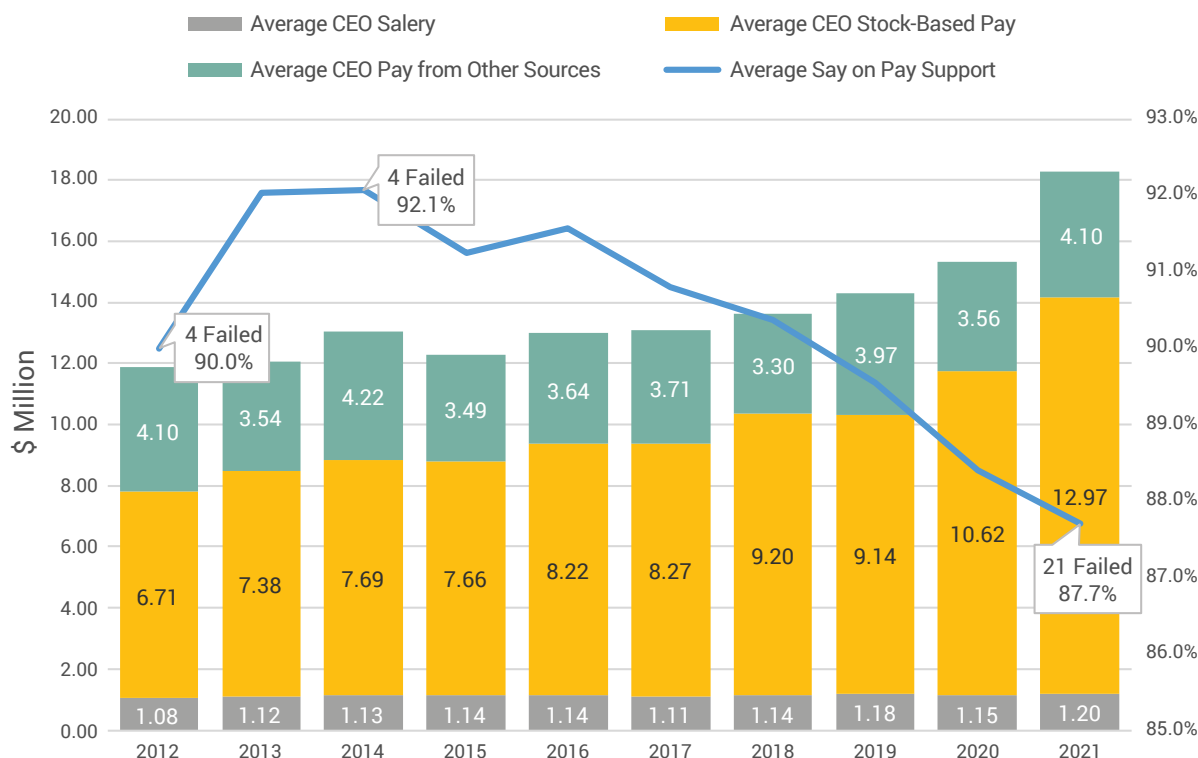
<https://theconversation.com/strikes-why-soaring-ceo-pay-could-help-explain-uks-recent-industrial-action-192709>

20. Corporate Secretary (2022). Executive Compensation: Insight on companies' governance, accessed (24.01.23).

<https://www.corporatesecretary.com/content/executive-compensation-insight-companies%E2%80%99-governance>



Chart 1: 10-Year Growth in S&P 500 CEO Pay v. Average Say on Pay Support



Ahead of the 2023 proxy season, the UK Investment Association recommends that remuneration committees show restraint: they should consider salary increases below the rate offered to all employees and dial down variable pay increases offered under any new policies. For payouts under long term incentive plans adopted in 2020, the investor representative body recommends that boards consider whether earlier, possibly overly modest, targets set under the cloud of the pandemic could lead to windfall gains for 2022 that stand in stark contrast with the hardships of the broader UK workforce.²¹

Shareholders Weigh ESG-alignment of Incentive Pay

Surveys of pay practices show rapid uptake of ESG-linked incentive pay. In 2020, 42 of the largest 100 European companies included an ESG metric in their variable remuneration plans.²² In 2021, 57% of S&P 500 companies incorporated ESG considerations. Globally, 44% of governance professionals recently polled confirm that their board incorporates ESG metrics into executive pay, with 60% for European boards.²³

While investors generally support this trend, and academic research shows an encouraging link between ESG incentives and ESG performance, the devil is in the detail. For instance, do large oil and gas companies that have introduced emissions reduction targets continue to also incentivize increased fossil fuel production growth? Moving beyond the simple question of whether a company has ESG performance pay metrics, investors will be considering factors like target levels, measurability, materiality, overall weighting, and the period over which incentives apply.

The Sustainability ESG Voting Policy Overlay’s climate governance voting strategy, implemented in 2022, sets rigorous expectations for heavy emitting companies’ climate-linked pay incentives when recommending votes on pay approval. The voting strategy focuses specifically on emissions reduction targets contained in the pay plans of large polluters. We recommend voting against approval of pay practices that do not track meaningful Scope 3 emissions targets.

21. The Investment Association (2022). IA Principles of Remuneration and Shareholder Expectations for 2023, accessed (24.01.23). https://cdn.roxhillmedia.com/production/email/attachment/1090001_1100000/e90974a6740e6d568efdcc3171a75750192b43b5.pdf
 22. Deloitte (2021). Insights into executive remuneration at Europe’s largest companies, accessed (24.01.23). <https://www2.deloitte.com/content/dam/Deloitte/uk/Documents/tax/deloitte-uk-europe-remuneration-report.pdf>
 23. Corporate Secretary, Executive Compensation.



5. COP 15 Puts Biodiversity Targets into Corporate Strategy

With the adoption of the [Kunming-Montreal Global Biodiversity Framework](#) (GBF) by 196 nations in December 2022, companies will come under greater pressure to pursue strategic targets for eliminating biodiversity loss from their operations and supply chains and for shifting towards nature-positive modes of business.

The GBF, which enjoys strong investor support, commits member states to halting and reversing biodiversity loss by 2030. Specifically, it sets a high-level target of protecting 30% of Earth by 2030 – including coastal and marine areas. It also requires that member states undertake restoration of 30% of the world's degraded lands and waters by 2030. Importantly, the deal involves redirecting financial flows; nations are to cut nature-damaging subsidies to the tune of USD 500 billion by 2030, as well as mobilize financing for national biodiversity strategies and action plans by up to USD 200 billion per year by 2030.

Notably, private finance is expected to contribute significantly to reversing biodiversity loss through various mechanisms, including leveraging private finance, promoting blended finance, implementing strategies for raising new and additional resources, and encouraging the private sector to invest in biodiversity, particularly through impact funds and other instruments.

As with climate action, investors are sharpening their focus on the investment risks of natural capital degradation, and they're also sharpening their tools for engagement. The guidebook for effective investor stewardship on tackling nature loss and biodiversity does not have to be written from scratch, and this promises an accelerated timescale for biodiversity action.

Supporting the governance shift, the International Corporate Governance Network, or ICGN, put out a statement on the Governance and Stewardship of Biodiversity Responsibilities for COP 15²⁴, which lays out expectations for investors, companies, and auditors. It recommends companies adopt science based targets on contributions to stabilizing biodiversity loss by 2030, and to ecosystem restoration by 2050; ensure robust governance procedures and board competence; and align corporate purpose and senior executive pay and incentives with “quantifiable financial, human and natural capital-related performance metrics.”

Adapting the collaborative climate stewardship framework, a coalition of institutional investors launched [Nature Action 100](#) in the days prior to the signing of the COP 15 accord, led by large institutional investors with global assets and by investor networks active in mobilizing investor climate action.

Adapting the TCFD climate disclosure framework, the investor-led [Taskforce on Nature-Related Financial Disclosures](#) (TNFD) - consisting of investors, corporations, and service providers - released an early version of a new reporting framework and risk management standards. The market release of the full framework is planned for September 2023. One of the principles on which the framework is built recognizes the climate-nature nexus.

24. International Corporate Governance Network (2022). Statement on the Governance and Stewardship of Biodiversity Responsibilities COP15, accessed (24.01.23). <https://www.icgn.org/statement-governance-and-stewardship-biodiversity-responsibilities-cop15>

Extending the model of the [Science Based Targets Initiative](#) (SBTi) for climate target setting, the collaborative Science Based Targets Network (SBTN) aims to sharpen companies' target setting and measurement approaches for making progress along scientifically recognized pathways that reverse nature loss.

Shareholder resolutions are another tool in the investor nature action toolbox. Several high-profile ballot successes in 2022 reveal investors' growing commitment to stem natural capital degradation and will give biodiversity engagements with companies even more momentum in 2023.

Table 2: Environmental Stewardship on the Ballot in 2022

Company	Title	Management's Vote Recommendation	Sustainalytics' Vote Recommendation	Reported Support	Independent Shareholder Support
<i>Report on Sustainable Packaging Efforts to Reduce Plastic Use</i>					
Amazon.com Inc	Retailing	Against	For	48.92%	59.24%
General Mills, Inc.	Food Products	Against	For	56.49%	56.68%
Jack in the Box Inc.	Consumer Services	Against	For	95.41%	95.41%
McDonald's Corp	Consumer Services	Against	For	41.88%	41.88%
Metro Inc.	Food Retailers	Against	For	30.14%	30.14%
Sysco Corp.	Food Retailers	For	For	92.09%	92.09%
The Kroger Co	Food Retailers	Against	For	38.37%	38.37%
Tyson Foods Inc	Food Products	Against	For	13.66%	57.11%
<i>Report on Business Impact of Shift Away from Virgin Plastic Production</i>					
Exxon Mobil Corp.	Oil & Gas Producers	Against	For	36.47%	36.47%
Phillips 66	Refiners & Pipelines	Against	For	50.37%	50.37%
<i>Eliminate Deforestation from Supply Chains</i>					
Home Depot	Retailing	Against	For	64.70%	64.70%
<i>Report on Water Stewardship</i>					
Alphabet Inc	Software & Services	Against	For	22.60%	61.50%
Tesla, Inc.	Automobiles	Against	For	35.40%	47.93%
<i>Report on Preservation of Biodiversity</i>					
Metro Inc.	Food Retailers	Against	For	37.09%	37.09%



6. Sustainalytics' ESG Voting Policy Updates

6.1 Climate Transition Plan Analysis

More and more companies are presenting their Climate Transition Plans (CTP) to shareholders, formulating greenhouse gas (GHG) emissions reduction targets and roadmaps for their achievement. To evaluate a CTP proposed for a vote (or 'say-on-climate' proposals), Sustainalytics' ESG Voting Policy Overlay team has developed a set of criteria, in line with international standards and investor expectations.

In 2022, the team evaluated 37 climate transition plans in recommending votes on companies' 'say on climate' resolutions. We also analyzed the climate targets and, where relevant, action plans of another 70 large fossil fuel companies in evaluating whether senior incentive pay is aligned with credible climate targets.

In order to achieve the goals of the Paris Agreement, it is essential for companies to have a defensible climate transition plan and to disclose to investors the roadmap and timeline for achieving GHG emissions reduction commitments, including full value chain emissions, in line with the global net zero goal. In 2022, we paid particular attention to the inclusion of Scope 3 targets in climate plans, for companies where such emissions are material.

Governance of climate change risks is another important consideration when evaluating a CTP. We expect companies to establish board- and executive-level oversight of climate risks and emissions reduction strategies, as well as to incorporate climate targets in executive remuneration schemes.

Starting from 2023, our evaluation of CTPs will include an expectation for companies to perform a scenario analysis for physical, financial and transition risks, including the disclosure of temperature rise assumptions. Such analysis benefits shareholders by providing better transparency into companies' readiness to face various temperature rise scenarios, and helps companies better prepare for the future.

Strong Climate Transition Plans should:

Take into account widely recognized decarbonization pathways

Set independently-verified science based emission reduction targets, including short-, medium- and long-term targets

Set a target for Scope 3 emissions reduction, where material

Include appropriate governance measures to support the transition

Include scenario analysis for physical, financial and transition risks

Be reported in line with the TCFD framework

6.2 Engagement Escalation Guidelines

Investors recognize that engagement is based on a shared commitment between companies and their investors to mitigate ESG risks, enhance resilience and build long-term value. However, effective engagement often takes place in the shadow of an escalation strategy that may be activated should companies resist engaging with shareholders or fail to make progress towards mutually understood milestones within a reasonable timeframe.

Sustainalytics' ESG Voting Policy Overlay, or signals incorporates engagement escalation as one of four ESG voting strategies, or signals. The objective of this voting strategy is to identify companies with weak engagement track records and to translate investor concerns into votes on key governance-linked ballot initiatives.

In a collaboration between engagement managers and the voting research team, Sustainalytics' Stewardship Services has refined a formal voting escalation procedure, codified in a set of internal guidelines, that add valuable escalation tools to the investment stewardship toolbox, enhancing the continuity between engagement and voting.

When ongoing engagement efforts are not making sufficient progress according to a clear set of criteria, an engagement manager may flag a company to the ESG Voting Policy Overlay team to escalate the engagement by recommending a vote against one or more management-sponsored ballot items at an engagement company's upcoming AGM. The process takes into consideration the engagement dialogue, the engagement objectives, the company's response, and the timing of the AGM in relation to ongoing engagement activities.

To be effective, escalating an ESG concern to voting against management should include clear communication about the escalation process and about the reasons for taking specific voting positions. Several stages to the process create opportunities for communicating with the company over the proposed escalation, both prior to and following the AGM.

We believe our new process keeps the engagement model at the forefront of investment stewardship practice.

Proxy Voting Escalation Process



Appendix 1: 2022 Regulatory Developments Impacting Corporate Accountability and Proxy Voting

International

[ISSB Issues Proposals for Sustainability- and Climate-Related Reporting Standards](#)

31 March

IFRS S1 for sustainability-related financial reporting and IFRS S2 for climate-related reporting are intended to capture information on a company's governance, strategy, risk management, and metrics and targets. The standards build on the TCFD framework with the aim of establishing a global baseline for sustainability-related disclosures. After a consultation period ending in July, the ISSB has subsequently confirmed requirements for Scope 3 GHG emissions reporting and the use of climate-related scenario analysis in IFRS S2.

EU

[European Commission Publishes Draft Corporate Sustainability Due Diligence Directive \(CSDDD\)](#)

23 February

The proposed CSDDD would require EU-registered companies and non-EU companies operating in the EU: to undertake human rights and environmental due diligence assessments of negative impacts, both direct and in the value chain; to set up necessary governance arrangements and mitigation plans; and to face sanctions for non-compliance. The specifics are being negotiated in Parliament, with the final report anticipated in May 2023.

[European Parliament Adopts Corporate Sustainability Reporting Directive \(CSRD\)](#)

10 November

The CSRD will replace the Non-Financial Reporting Directive (NFRD) in effect since 2018, extending sustainability reporting obligations to a wider set of companies, including non-EU parents with operations in the EU, and a broader range of topics, taking a double materiality approach. Companies will be required to obtain independent verification of reported information. The first set of reporting standards under the CSRD will be adopted by June 2023.

[EFRAG Adopts Draft European Sustainability Reporting Standards \(ESRS\)](#)

23 November

The European Financial Reporting Advisory Group (EFRAG) submitted the first set of draft standards for sustainability reporting under the CSRD mandate to the European Parliament for consultation and anticipated adoption in June 2023. They lay out general cross-cutting requirements under the new CSRD reporting framework as well as specific reporting requirements for environmental, social and governance topics. A subsequent set of draft standards will tackle sector-specific disclosure standards.

[European Parliament Adopts 'Women on Boards' Directive](#)

22 November

The Directive to enhance board gender diversity will require that, by July 2026, the boards of large listed companies in the EU must balance the representation of each gender by at least 40% among non-executive directors, and 33% among all directors. Companies will be required to annually report board gender breakdown, and explain why targets have not been met, where relevant.

Australia

[Australian Govt Initiates Consultation on Mandatory Climate-Related Financial Reporting](#)

12 December

In late 2022, the Australian Treasury released a consultation paper on the development of a climate risk disclosure framework that would align with international frameworks and would form part of the development of a broad sustainable finance framework for Australia.

Canada

[Standards Bodies Approve Proposal for Canadian Sustainability Standards Board \(CSSB\)](#)

15 June

In June, a proposal by the Independent Review Committee on Standard Setting in Canada (IRCSS) for the formation of the CSSB as a Canadian counterpart to the ISSB was approved. The board will be formed in April 2023 with the task of feeding Canadian interests into international standard setting as well as reviewing, endorsing, and adapting international sustainability standards for use in Canada.

Japan

[Japan's Financial Services Agency \(FSA\) Proposes ESG Disclosure Regulation](#)

19 December

The FSA's proposed amendment to the Financial Instruments Exchange Act of Japan requires that Japan-listed companies disclose additional ESG information for fiscal years ending on 31 March 2023 or later. Disclosures would cover gender diversity, as well as sustainability governance and risk management frameworks, using pillars that map to the TCFD framework.

Switzerland

[Switzerland Adopts Mandatory Climate Reporting Law](#)

23 November

Switzerland's newly adopted "Ordinance on Climate Disclosures" law, effective from January 2024, will require large public companies, banks and insurance companies to provide TCFD-aligned reporting.

UK

[UK Parliament Passes Law Mandating Climate Related Financial Disclosures](#)

17 January

Effective for financial years starting on 6 April 2022, the Companies (Strategic Report) (Climate-related Financial Disclosure) Regulations 2022 will require large UK companies to produce TCFD-aligned climate-related financial disclosures in the Non-Financial Information Statement of annual reports - now called the Non-Financial and Sustainability Information Statement.

[UK TPT Publishes Consultation on Transition Plan Reporting](#)

15 November

In April, the UK Treasury launched the Transition Plan Taskforce (TPT) with the aim of developing a gold standard for private sector climate transition plans. With the release for consultation of the TPT Disclosure Framework and TPT Implementation Guidance, companies will have an opportunity to test implementation before the Framework and Guidance are finalized.

[Parker Review Publishes Updated Findings on the Ethnic Diversity of UK Boards](#)

16 March 2022

The 2017 UK government-backed Parker Review established the target that each FTSE 100 Board should have at least one director from a minority ethnic group by the end of 2021 and, for FTSE 250 boards, by the end of 2024. The 2022 Update Report finds that 89 of the FTSE 100 and 55% of FTSE 250 companies have, so far, achieved this target.

US

[SEC Proposes Rules to Enhance and Standardize Climate-Related Disclosures](#)

21 March

Proposed climate reporting rules would require companies to provide investors with standardized reporting of physical and transition risks; net zero transition plans, including governance arrangements; and GHG emissions, including Scope 3 emissions where material. While a final rule has been delayed from the initial October target, and it faces anti-ESG pushback, companies may already be adjusting their disclosures in anticipation of stronger climate reporting rules in the near future.

[SEC Proposes Amendments to Shareholder Proposal Rule](#)

13 July

Proposed shareholder proposal rule amendments aimed at narrowing three bases on which companies may exclude shareholder resolutions from their ballots effectively gives shareholders more options for filing ESG resolutions, counteracting restrictions on resolution filing adopted in 2020.

[SEC Adopts Pay Versus Performance Disclosure Rules](#)

25 August

Proxy reports for fiscal years ending after 16 December 2022 should now contain standardised information on how compensation actually paid to senior executives relates to a company's financial performance, helping investors to better evaluate incentive pay over the most recent three years in 2023, extending to five years by 2025.

[SEC's Universal Proxy Rule comes into effect](#)

1 September

Investors waging proxy contests can put their candidates on management's proxy ballot alongside the board's own nominees, allowing investors to select among individual candidates from a combined slate and likely spurring more competition for board seats. ESG factors are likely to become more relevant to proxy contests.

[SEC Adopts Enhancements for Vote Reporting by Investment Funds and Managers](#)

2 November

Enhancements to Form N-PX proxy voting disclosures will require registered funds to file more user-friendly voting reports and will require a broader group of institutional investment managers to disclose their say-on-pay votes, making it easier for shareholders to assess the voting practices of their investment fiduciaries.

[DOL Adopts Rule Amendments to Remove ESG Investing Barriers in Retirement Plans](#)

22 November

The US Department of Labor's amendments to fiduciaries' "Investment Duties" under the law governing the operation of worker retirement plans clarifies that plan fiduciaries may consider ESG factors when making investment decisions, such as proxy voting. This rule effectively overturns 2020 amendments that had sought to deter the consideration of ESG factors in retirement plans.

List of Acronyms

AGM: Annual General Meeting of shareholders

CSR: EU Corporate Sustainability Reporting Directive

DOL: US Department of Labor

ESRS: European Sustainability Reporting Standards

FRC: UK Financial Reporting Council

ICGN: International Corporate Governance Network

IFRS: International Financial Reporting Standards Foundation

ISSB: International Sustainability Standards Board

NFRD: EU Non-Financial Reporting Directive

SEC: US Securities and Exchange Commission

SRD II: EU Shareholder Rights Directive 2

TFC: Taskforce on Climate-Related Financial Disclosures

TPT: UK Transition Plan Taskforce



Do you have any questions regarding our
Stewardship Services?

Contact us today to connect with our team of experts.

Learn More About Sustainalytics

overlay.support@sustainalytics.com

engagement.support@sustainalytics.com

Europe: Amsterdam (+31) 20 205 00 00 | Copenhagen (+45) 32 72 52 81 | London (+44) 20 3514 3123

Frankfurt (+49) 69 3329 6555 | Paris (+33) 1 184880642 | Stockholm (+46) 8 505 323 33

Americas: Boston (+1) 617 603 3321 | New York (+1) 212 500 6468 | Toronto (+1) 416 861 0403

Asia Pacific: Sydney (+61) 2 8320 9436 | Tokyo (+81) 3 4510 7979



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