NEUBERGER | BERMAN

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Commitment on Climate

Our Engagement Series presents insights and case studies highlighting our dialogue with companies, government entities and other issuers of securities. In this column, Andrew J. Pritti and Dina Ciarmatori, research analysts for the Neuberger Berman Sustainable Equity team, explore the team's recent, successful engagement with a major software provider on the measurement and reduction of carbon emissions.

To the Sustainable Equity team, engagement is an essential tool, driving investment returns and supporting business sustainability. While engagement can result in immediate changes, such as greater transparency in financial disclosures or a better-qualified slate of directors for board seats, the potential for longer-term rewards is even greater. Over a multiyear time horizon, we have historically found that the lasting impact of engagement can reverberate and deepen to meaningfully shape corporate behavior in ways that enhance company results and create value.

Engaging With an ESG Standout

In this case, the company we engaged with has been part of our portfolios for the better part of two decades. It is a leading provider of business and financial management solutions for an array of companies and financial institutions, and has proven adept at broadening its reach into underserved markets, a trend that continues today as it shifts to a cloud-based business model. The mission of the company is "to power prosperity around the world."[1]

Underlying its financial success, the company has been a standout on ESG issues. For the last 17 years, it has been recognized as one of *Fortune's* "Best Companies to Work For,"[2] and was more recently named to the *Forbes* "America's Best Employers for Diversity"[3] list. With a workforce of 9,000, it successfully conducted and published the results of its gender pay gap analysis since 2017, which helped to identify and close compensation differences between men and women. This has supported its ability to attract and retain talent, and underscores its meritocratic culture.

[1] Source: www.intuit.com.
[2] *Fortune* 100 Best https://fortune.com/best-companies/.
[3] https://www.forbes.com/lists/best-employers-diversity.

Key Concern: Energy Sourcing

One of the material environmental issues for technology and software companies is the emissions generated from energy use.

As with many technology companies, most greenhouse gas emissions come from this provider's use of electricity ("scope 2 emissions" in industry parlance[4]). Industry-wide, as of 2017, data centers account for roughly 2% of total U.S. electricity usage.[5] As technology advances and processing power increases, energy use is likely to increase. Indeed, information and communications technology could account for up to 14% of global emissions by 2040, rivaling the impact of the transportation sector.[6] As a result, it's becoming more important to tap renewables for energy-intensive data centers.

As part of our ongoing engagement, we have communicated regularly regarding the company's environmental strategy, including emissions reductions, use of renewable energy and setting improvement targets. Given our understanding of its business and the evolving competitive landscape, we made the business and environmental case for why we believe management should seriously consider setting explicit science-based targets (see box).

Specifically, our outreach on this issue took the form of a letter to the CEO and lead outside director. This led to a series of calls and meetings where we engaged in a dialogue and explained what we believe are the advantages of this more precise form of measurement and control.

Company management decided to take a closer look to better understand this process. In early 2019, it agreed to set science-based targets and seek approval for those targets with the Science-Based Target Initiative ("SBTI"),[7] which administers the standard.

Subsequently, in April 2019, the SBTI approved the submission, which included a commitment to reduce absolute "scope 1, 2 and 3" greenhouse gas emissions 50% by 2025 from 2012. The company also agreed to increase its annual sourcing of renewable electricity from 32% in 2015 to 100% by 2030. Both goals are consistent with the global goal of limiting global warming to 1.5°C, as articulated in the Paris Agreement.[8]

A Continuous Effort

The outcome was particularly meaningful, as the company was very receptive to our engagement efforts, which ultimately led to action. We recognize, however, that our task as active investors is a marathon, not a sprint, which requires broad comprehensive effort. We reach out regularly to all of our portfolio holdings regarding ESG concerns, advocating best practices and a forward-looking, strategic-minded approach to head off potential challenges and get ahead of potential opportunities. We may be a sole voice on a particular issue, or part of a collective effort to initiate and encourage change. In all of our engagements, our primary goal is to drive a higher level of management attention to key ESG issues that we believe have the potential to improve the long-run competitive position of the companies in which we invest.

[4] Scope 1 emissions are direct emissions from owned or controlled sources. Scope 2 are direct emissions from the generation of purchased energy. Scope 3 encompasses the entire value chain, from goods purchased to the disposal of products sold.

[5] Source: U.S. Department of Energy, https://www.energy.gov/eere/buildings/data-centers-and-servers.

[6] Source: Lotfi Belkhir and Ahmed Elmeligi, "Assessing ICT Global Emissions Footprint: Trends to 2040 & Recommendations," *Journal of Cleaner Production* (2018).

[7] Targets adopted by companies to reduce greenhouse gas (GHG) emissions are considered "science-based" if they are in line with what the latest climate science says is necessary to meet the goals of the Paris Agreement: to limit global warming to well below 2°C above pre-industrial levels and pursue efforts to limit warming to 1.5°C. The Science-Based Targets Initiative (SBTI) is a collaboration between CDP, the United Nations Global Compact (UNGC), World Resources Institute (WRI) and the World Wide Fund for Nature (WWF), and is one of the We Mean Business Coalition commitments. The initiative's overall aim is that, by 2020, science-based target setting will become standard business practice and corporations will play a major role in driving down global greenhouse gas emissions. Companies can work with the SBTI to set and gain approval of their science-based targets.

[8] The Paris Agreement is an agreement within the United Nations Framework Convention on Climate Change, dealing with greenhouse-gas-emissions mitigation, adaptation and finance, which was signed in 2016.

Understanding Science-Based Targets

When it comes to climate, we believe that more precise measurement enhances accountability. Science-based targets specify how much and how quickly companies need to reduce their greenhouse gas emissions in order to be consistent with the Paris Agreement's central goal of limiting the current century's global temperature increase to 2°C above pre-industrial levels, or, more aggressively, limiting warming to 1.5°C.

Beyond contributing to broader environmental goals, we believe implementation of such targets provides companies with a competitive advantage in the transition to a low-carbon economy. According to a recent survey conducted by the Science-Based Targets Initiative, some 63% of corporate respondents said that science-based targets are helping to drive innovation at their companies.[9]

[9] Source: https://sciencebasedtargets.org/.

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