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Voting the Votes: Materiality and Shareholder Proposals One Year On

Before the 2018 proxy voting season began, we laid out our commitment to integrating the Sustainability Accounting Standards Board's (SASB) guidance on materiality into our evaluation of the proxy votes that we cast on behalf of clients (see "From Talking the Talk to Voting the Votes"). With the bulk of the season now behind us, we offer below six shareholder proposals where a materiality-driven evaluation assisted us in our voting decision. These examples represent just a portion of our views on the subject—which we expand upon in our annual Engagement and Proxy Voting Report

We have focused on the SASB standards because they represent a decision-useful, investor-focused framework. Our analysts were involved in the standards development process from the start, and we continue to support the maintenance of the standards as members of the SASB Sector Advisory Groups. We have been clear about how we use the standards because accountability works both ways—while investors expect issuers to successfully manage environmental, social and governance (ESG) risks and opportunities, issuers should expect that investors clearly communicate their preferences on the management of those topics. The following examples illustrate how the SASB standards serve as a useful tool not only for evaluating a shareholder proposal, but also as a lens for performing further analysis and engagement.

Political Lobbying and Disclosure

Neuberger Berman Voting Guideline: "Given the potential reputational impact of the use of company funds in relation to trade associations and political processes, Neuberger Berman will generally support shareholder proposals asking for disclosure and/or reports on this issue."

The topic of political lobbying and its disclosure deserves more complete treatment in a future publication. For now, however, we use as an example the SASB Materiality Map on elements of Leadership and Governance related to "Management of the Legal & Regulatory Environment." which includes how a company "influences the regulatory or legislative process and outcomes, including whether an issuer's stance may align with or differ from the official stance of its industry organization(s)".

In one instance, an oil and gas company received a shareholder proposal requesting the preparation of an annual report on procedures and expenditures made to political organizations, a likely material issue under SASB standards for that industry. While many companies, including this one, already offer such disclosure, the oil and gas industry in particular faces reputational risks related to the intention—or the appearance of intention—to influence regulators through various trade groups and organizations, some of which have attracted significant negative public attention and the departure of prominent corporate members. The company in this example does not disclose its involvement with political organizations that draft model legislation, and we felt shareholders would benefit from transparency in this area. As such, we decided to support the shareholder proposal, which received more than 30% of shareholder votes.

A similar proposal was made at another oil and gas company that disclosed its memberships in various organizations but did not detail its payments to them. We supported the proposal there as well. While the compilation and disclosure of this data may appear onerous to issuers, we believe strongly that shareholders have the right to understand the reasons behind management's deployment of shareholder capital and whether sufficient consideration is given to the risks that political involvement introduces to the sustainability of shareholder value.

The issue of trade associations also appeared on the proxy for an electric utility company, another industry where "influencing the regulatory or legislative process and outcomes" is likely to be material under the SASB standards. Consistent with our views on similar measures at other companies, we initially were inclined to support the proposal; closer analysis of the proposal's intent, however, led us to conclude that it would not be in the best interest of shareholders. An important part of our evaluation process entails separating a proposal's substance from the intention of its proponent, which enables us to evaluate a proposal on its own merits. In this particular instance, we were concerned that adoption of the proposal would lead to misuse by directing the company to cease participation in all industry organizations; in contrast, we sought disclosure of all company activity in this area and the cessation only of those activities that create unnecessary risk. In general we expect companies to align any political/lobbying expenditures with the strategy management has articulated to shareholders and to closely scrutinize the work that is conducted on their behalf by the organizations they fund. This example as well as related campaigns and efforts, both old and emerging, of "greenwashing" are closely scrutinized in our shareholder proposal evaluation process.

Environmental Impact

Neuberger Berman Voting Guideline: "We will generally support shareholder proposals asking for increased disclosure [on environmental issues] where our assessment finds that existing materials are significantly lagging behind recognized frameworks necessary for investors to assess these risks."

Shareholder proposals related to the environmental impact of companies continued to be commonplace this year. SASB's identification of the following material and immaterial issues for a restaurant company helped us evaluate a shareholder proposal related to single-use plastics:

- Waste and hazardous materials management – likely material
- Biodiversity impacts – likely immaterial
- Product packaging – likely material

Because the scope of this proposal spanned several environmental categories with varying levels of materiality to the business, a more nuanced evaluation was necessary. Ultimately we determined that the shareholder proposal was material to the continuing operations of the business because of both shifting consumer preferences as well as self-identified litigation and regulatory risks posed by the company's use of single-use plastics. However, our inquiry into the company's practices confirmed that it had done substantial work on this topic and had presented concrete plans to help shareholders understand the progress that it had made. Comfortable with management's plan and efforts to date, we did not support the proposal. Shortly after the shareholders' meeting, the company accelerated its timelines to reduce the environmental footprint of its plastics use.

A shareholder proposal at another restaurant company—this one concerning deforestation and land use—also failed to earn our support. While we generally believe deforestation and land use to be a salient topic and have participated in collaborative engagements on it, issuer materiality remains the determining factor. SASB does not identify these impacts as likely material to restaurant companies, and having examined the potential risks at this particular company, we were satisfied with the existing programs in place to successfully manage the issue. Generally, we feel issues such as these are best managed through collective engagement by shareholders.

The above two cases contrast with a shareholder proposal regarding a water-stewardship policy submitted at a meat, poultry and dairy producer, an industry in which all of the below are identified by SASB as likely or potentially material:

- Water and wastewater management – likely material
- Waste and hazardous materials management – likely material
- Biodiversity impacts – likely material
- Environmental, social impacts on assets and operations – potentially material

Though the company has made various commitments to address its water stewardship and has been making progress on both standardizing its reporting and improving its processes, the highly material nature of the proposal to issuers in the sector led us to conclude shareholders would benefit from explicit disclosure of this company's policies and procedures.

Growing Industry Consensus

We continue to believe that shareholder proposals represent an important channel through which shareholders may communicate material concerns to the Boards and management teams at companies.

To this end the SASB framework gives us an effective and consistent starting point for differentiating between shareholder proposals, and then prioritizing which proposal to conduct deeper and more nuanced analysis on. We will continue to seek to support shareholder proposals that are well written and intend to mitigate material ESG risks at the specific company, or to provide shareholders with actionable disclosure which is relevant to the specific company.

We will continue to refine our analytical processes and to engage directly with issuers on our views about material ESG topics—it is incumbent on both sides to identify the right issues and have their voices heard. Since we announced the integration of expectations around SASB into our Proxy Voting Guidelines in early 2018, we have been pleased to see other asset managers and some proxy advisory firms follow suit. We view this as an important signal of the growing consensus among investors about how important it is for companies to focus on disclosing and managing material sustainability issues.

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