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2020 Proxy Voting Season Review: Beyond 'business as usual'

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Executive summary

- The global COVID-19 pandemic brought disruption to voting season across Europe, North America and Japan. Companies struggled to host in-person meetings, but many quickly moved to hold virtual AGMs, aided by technology. We believe that a hybrid system – where physical meetings are enhanced by full online capability – could boost shareholder participation, particularly for international investors.

- The pandemic has forced many companies to ask themselves what they stand for beyond profit – what their 'corporate purpose' is and how this is integrated into every facet of business.

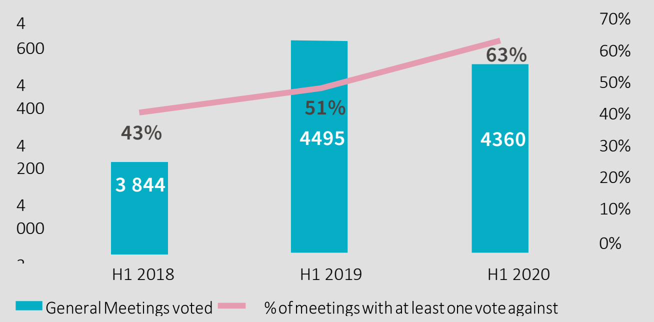
- COVID-19 has also highlighted the importance of board oversight of management. Executives have been forced into quick decisions to cope with the short-term impact of the pandemic but thoughtful consideration must be given to the longer-term implications, and to the need to keep shareholders informed.

- We expect two trends to gain prominence as we move past the crisis. First, a rise in employee activism, where staff take their companies to task on human rights, environmental issues, social concerns, and employee relations. Second, the question of pay 'fairness' as more companies disclose data on the ratio between CEO pay and median employee pay.

COVID-19 has had an unprecedented impact on the world economy. The crisis also coincided with peak of the proxy voting season – the period between March and June when the majority of listed companies hold their annual general meetings (AGMs). Cognisant of the pandemic and its overall effects on both society and the economy, we observed that many of our pre-AGM engagements with investee companies had a strong ESG element to the discussion that went beyond the traditional voting issues usually discussed in more routine years.

That has been encouraging, and it is important too that in moments like this, investors do not drop their guard. During the first half (H1), we recorded a vote against management on at least one resolution at 63% of company meetings. This was a notable increase from last year. The data are discussed in detail in our 2020 H1 Active Ownership and Stewardship Report[1].

Graph 1: AXA IM 2020 voting (H1) number of meetings voted and level of dissent



[1] AXA IM H1 2020 Active Ownership Report. COVID-19: Stewardship and the pandemic

In addition, we enhanced our voting policy on key topics including board gender diversity, time commitment of directors, auditor rotation, and the integration of non-financial ESG metrics into executive compensation[2]. This has been a highly unusual AGM season for everyone involved, and it has thrown up some fascinating issues and trends to explore around engagement and governance. These include virtual AGMs, corporate purpose, director duties & responsibilities, employee activism, and executive pay.

Virtual AGMs

Social lockdowns imposed by governments globally curtailed companies' usual approach of holding in-person AGMs. While some companies postponed their AGMs, others moved to hold virtual, online meetings on an exceptional basis. This was very much the notable development of this year's proxy voting season. AXA IM is supportive of companies moving to virtual online meetings in emergency cases. We however encouraged companies to return to physical, in-person meetings once the COVID-19 situation normalises.

Virtual, online meetings help augment shareholder participation especially for international investors who can rarely attend in person. This is a positive for shareholder rights – but we also believe it is no permanent replacement for companies holding AGMs in person. In the UK we saw examples of companies putting forward article amendment resolutions that would potentially allow them to hold virtual-only meetings. However, these were either defeated[3] or passed with a very slim majority[4] suggesting that investors still harbour reservations about the prospect of virtual-only meetings post-pandemic.

The rapid shift to virtual AGMs could signal that corporate thinking and technology are now at a point where they can deliver so-called "Hybrid AGMs" – where a physical meeting is enhanced by a full online presence at the same time. These Hybrid AGMs could boost shareholder participation and allow international investors an effective means of participating. We expect this will become increasingly commonplace in future years.

Corporate Purpose

Few topics this year have caught the attention of shareholders and stakeholders quite like the idea of 'corporate purpose'. It has become ever more important as the world deals with a generation-defining crisis. What do companies stand for? How do they define themselves beyond profit alone? How is this reflected in their dealings with employees, shareholders, supply chains, stakeholders and the environment?

In 2019, France's PACTE law[5] introduced a provision on the legal responsibilities of the board of directors. French law has long said companies should be managed according to the 'social interest', but the PACTE law goes one step further. It requires boards to take into consideration the social and environmental effect of a company's activities while fulfilling their fiduciary duties. The law also introduced the concept of corporate purpose, with implementation possible through the amendment of bylaws or formal statements to boards and shareholders.

On the other side of the Atlantic, the US Business Roundtable (BRT), a non-profit composed of CEOs of American corporations, issued a statement defining a corporation's purpose as working for the benefit of all stakeholders. These two developments show a slow but certain shift from the shareholder primacy model to the stakeholder model of corporate governance and come alongside sustained growth in responsible investment and more demanding shareholder expectations around the management and reporting of ESG risks.

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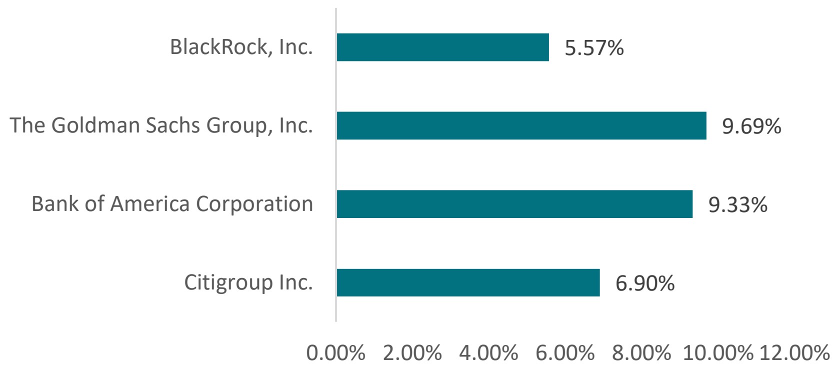
[2] AXA IM, 2020 Corporate Governance and Voting Policy Updates, 2020
[3] Standard Life Aberdeen, AGM Vote Results, 2020
[4] 888 Holdings, AGM Vote Results, 2020
[5] La loi PACTE : pour la croissance et la transformation des entreprises

It is still early days. The concept of corporate purpose remains a work in progress but like all governance evolutions, these first steps will shape how it is eventually defined. One recent survey showed[6] that a majority of investors expect companies to define their corporate purpose and push for some degree of tangibility in determining and reporting against it. Assuming continuous growth in responsible investment, we believe a corporate purpose that takes into consideration the wide stakeholder base will become the norm in the long run.

In 2019 and 2020, a majority of French main index (SBF 120) companies amended their corporate purpose following the PACTE law decree. Only a small number – nine – chose to do so through a bylaw amendment, but these resolutions received overwhelming support. Others issued board and executive statements to implement the law, or sought compliance through clarification/confirmation that the board takes into consideration the social and environmental impact of the company's activities when executing its fiduciary duties.

In the US, following the BRT statement, we saw a handful of shareholder resolutions asking boards to review or report on corporate purpose. Investor pressure on this is clearly in the early stages, and none received management backing. The level of support was therefore relatively modest compared to the evolution in France.

Graph 2: Support at U.S companies for shareholder resolutions asking for reporting or amending the statement of purpose



Source: AXA IM

As long-term stewards of assets for the investees we represent, we will be pushing companies to communicate on their process and progress towards defining and implementing their corporate purpose. In the US, the mere disclosure of sustainability reports is being considered enough proof that companies are taking the concept of corporate purpose seriously, but investors are increasingly demanding something more tangible.

This is starting to emerge in France, though marginally. One company we engaged with has taken into consideration its corporate purpose when determining its dividend distribution policy this year, and when determining the variable portion of executive remuneration. Other companies have decided to report specifically on their corporate purpose in their annual reports, including key performance indicators (KPIs) and linking to medium- and long-term strategic plans.

[6] Making Corporate Purpose Tangible—A Survey of Investors, Posted by Edouard Dubois and Ali Saribas, SquareWell Partners Ltd, Harvard Law School Forum on Corporate Governance

We will monitor this significant evolution in corporate governance practices, particularly as the concept expands to encompass the wider stakeholder base on an EU level. Already there are some key observations from our engagements during the first six months of the year:

- The corporate purpose goes beyond the duties of the board of directors: its determination is a company-wide effort involving multiple internal and external stakeholders.
- Formal bylaw amendments are still relatively uncommon, with companies choosing the less stringent legal framework available.
- Corporate purpose remains an intangible concept, though companies are starting to report against KPIs and some are including performance against corporate purpose KPIs in their variable remuneration.
- With legal changes in France putting environmental and social issues at the heart of the board's role, it has become very difficult to avoid clarifying the corporate purpose to take into consideration these factors.

Director Duties and Responsibilities in a Crisis

The COVID-19 pandemic has thrown a sharp light on the role and responsibilities of the board and its various committees. Chief among them is a board's responsibility to ensure robust oversight of management in dealing with the short-term impact of the pandemic and decisions made often at lightning speed, while ensuring the longer-term implications of decisions made today are thoughtfully considered.

The responsibilities of directors and the board include strategic direction, communication with stakeholders, and remuneration, among other topics, but a good board would also be actively participating in overseeing business continuity plans, the resistance of an organisation, and how the company positions itself once a 'new normal' is established following an easing of the pandemic.

One question is often raised. Should companies have done more to anticipate and plan for 'black swan' events as part of the normal course of audit, business risk, contingency and continuity planning at a board level and across risk functions (including the audit committee and or risk committees)? There are some who would say that boards could have done more[7], but it is difficult to consider that anyone could conceivably have predicted a scenario where the vast majority of the world was put into lockdown measures and where the nature of employment and the viability of entire industries was called into question[8].

In our engagement with companies, ahead of and after voting at an AGM, we have observed:

- Companies are keen to highlight their response to the COVID-19 pandemic and its consequences
- Directors are spending more time communicating with executives on the financial impact as well as operational logistics and strategic implications
- There remains a need to further bolster the role of the board and/or the risk and audit functions in anticipating and planning for future crises in whatever form they may come
- The possibility of exploring additional skillsets required on boards in the future.

When considering director duties we will watch closely as companies describe how they considered the consequences of any decision over the long term – how they considered the interests of employees, and the relationship with suppliers, customers and others. We will also pay attention to how companies considered the impact of their operations and actions on the community and environment, how they maintained high standards of business conduct, and ensured that they acted fairly across shareholders.

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[7] Louise Pentland, Paypal Executive and Hitachi Non-Executive Director. Covid - 19-crisis-and-its-aftermath-corporate-governance-implications-and-policy-challenge, 2020

[8] AXA IM, COVID-19: Has your workplace changed forever?, 2020

Employee activism - On the march

The pressure on companies to become more socially responsible has traditionally been linked to its shareholders, to regulators, and to governments. However, the past couple of years have seen more and more instances where employees take their own companies to task on human rights, environmental issues, social concerns, and employee relations. Employee activism is on the rise and appears to be here to stay.

Just as we as shareholders highlight the importance of a well-constructed corporate purpose, employees are increasingly demanding that the companies they buy from and the companies they work for take social and environmental factors into consideration along with profit. With the growth of social media, employees have a global platform to spread their message and amplify their voice far and wide before a company has a chance to react. A few examples of recent employee activism include:

Company	Issue
AMAZON	**Climate:** Amazon employees put a shareholder resolution onto the company's AGM agenda on climate issues[9]
WAYFAIR	**Human Rights:** Staff organised a walkout in protest at what they called the company's 'enabling, supporting, or profiting from' companies operating detention camps in the US[10]
ALPHABET	**Sexual misconduct allegations:** Employees walked out in protest at what they saw as the company's lenient treatment of those accused of sexual misconduct[11]
FACEBOOK	**Hate speech:** Employees staged a 'virtual' walk out in protest at the company's decision not to do anything about inflammatory posts made by the US President[12]

There are many other examples, including Amazon employees protesting the use of the company's AWS cloud computing division by the oil and gas industry, as well as continued protests over warehouse working conditions. There have also been concerns from tech company employees about the use of facial recognition technology by police, while Microsoft employees spoke out against the company's bid for a US Department of Defence contract (which it ultimately withdrew), and Google employees protested the company's work on a censored search engine in China.

At AXA IM, we believe that company employees are a critical and material driver of investor value creation[13]. As a result, we closely assess how companies engage with their staff. In our corporate governance engagements with companies it is clear that many are still getting to grips with how to deal with the rise of employee activism. We therefore note the following as good practice which we expect companies to follow:

- Ensure that a company's corporate purpose actually aligns with the actions it undertakes.
- Ensure that employee voices are heard across the organisation including at upper management and board level. It is no longer enough to run an employee survey once a year to gauge feedback. Companies have to do more to listen to the voices of staff.
- Be transparent. In this day and age information has a way of coming out no matter how tightly you try to control it. It is better for companies to be open about difficult topics than to try and manage the flow of information.
- Be comfortable that the values that you hold as a company also apply to your supply chain and, where relevant, to the customers and users of the products you sell.

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[9] CNN, 25 May 2019: Amazon climate resolution gets relatively strong showing despite failure

[10] Forbes, 2 July 2019: Wayfair Employees' Protest Of Sales To Detention Centers Could Backfire On Them

[11] The Guardian, 1 November 2018: Google walkout: global protests after sexual misconduct allegations

[12] BBC News, 1 June 2020: Facebook staff anger over Trump post

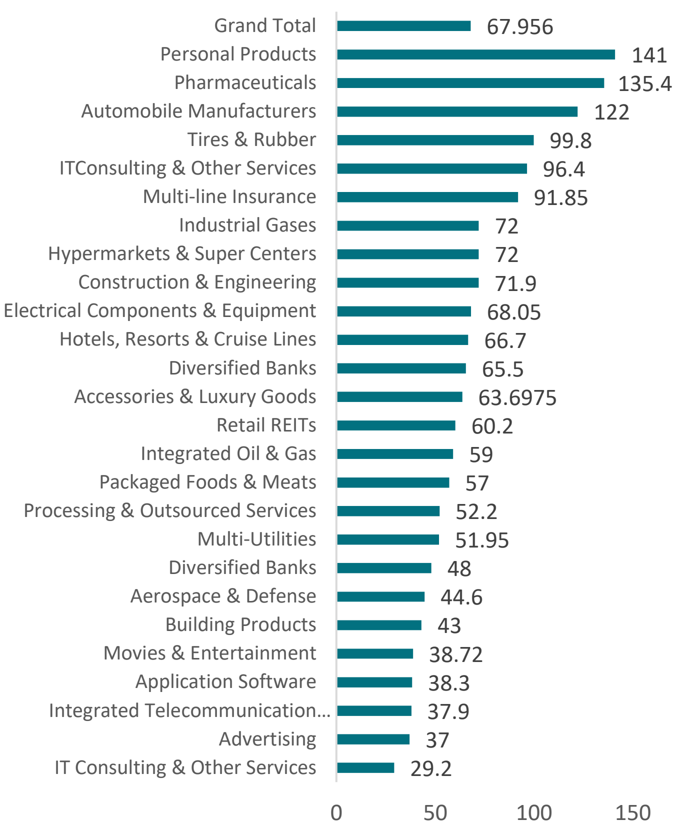
[13] AXA IM, Human Matters, 2018

- **Executive pay and rewards – Time to take stock**

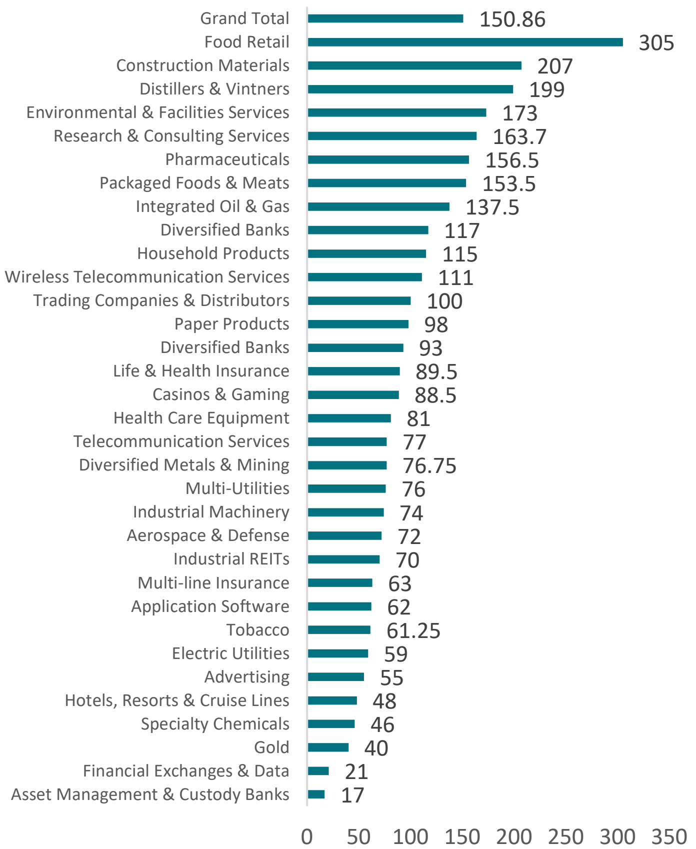
Corporate leaders often espouse the value of being 'in it together' to galvanise their employees, but when push comes to shove do these words actually mean much for executives when it comes to their pay? As a response to the COVID-19 pandemic we have seen a number of executives, across many industries, announcing pay cuts or forgoing part of their salaries and annual bonuses. Some of this has been done as a pre-requisite to securing state financial aid or in cases where companies have furloughed staff, while other companies have done so voluntarily. However, it remains to be seen whether this will translate into appropriate adjustments to bonuses and long-term incentives over the next 12 months.

It is also slowly becoming apparent, in markets where disclosure allows, that the CEO pay ratio – the ratio between CEO earnings and median employee earnings, is being used as a tool by employees and others to better understand the question of pay fairness across a company. The following graphic compares the pay ratio data for CAC 40 constituents and the 50 largest FTSE 100 companies:

Average of CEO pay ratio vs. median employee (*CAC 40*)



Average of CEO pay ratio vs. median employee (*50 largest UK companies*)



The importance of these ratios is growing such that investors are demanding increased transparency on the calculation methodology and are increasing the push for the pay ratio to be one of several important governance metrics in judging a company's overall ESG profile. The pay ratio will become one of several metrics investors factor in when judging a pay package's merits.

It is acknowledged that measuring pay for performance and comparing pay quantum to measures like the total shareholder return or other financial metrics have been an important part of analysing pay packages. The inclusion of pay ratios will bring an extra-financial consideration to the pay discussion, by linking pay practices to the company's general remuneration philosophy and to one of its most important stakeholders, its employees.