

# 2019 Corporate Governance Report



★ Segal Marco Advisors



# Introduction

Segal Marco Advisors (Segal Marco) serves more than 600 clients with advisory assets exceeding \$500 billion. In addition to financial consulting and discretionary services, Segal Marco provides proxy voting and corporate governance services. Segal Marco is a registered investment advisor and assumes fiduciary duty for proxy voting assets.

The *Corporate Governance Report* summarizes the market environment for corporate governance; the 2019 proxy votes on the most common issues, including proxy voting statistics; and Segal Marco's 2020 Proxy Policy Statement.

There are four updates to Segal Marco's Proxy Policy Statement that take effect in March 2020:

1. Segal Marco will vote against CEOs who are also serving concurrently as the board chair. Segal Marco has long supported independent board chairs and voted in favor of shareholder proposals seeking policies in support of one. We have also voted against insider directors where the board fell short of a two-thirds threshold for independence. The new policy extends and reinforces our perspective on director independence.
2. Segal Marco will enact a stricter over-boarding standard for CEOs. Segal Marco votes against corporate directors that serve on too many boards to be effective. Historically, we have applied the same threshold to CEOs and non-CEOs.
3. Segal Marco will classify directors serving on the same company's board for more than 10 years as insiders (referred elsewhere in this report as "non-independent directors"). Such long-serving directors may add valuable expertise but will be counted as insiders to ensure boards have appropriate levels of refreshment and independent perspective.
4. Segal Marco will vote against the nominating committee of board of directors with fewer than two women. This policy raises the threshold set in 2017 to oppose nominating committee members of boards with no women represented.

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## **Maureen O'Brien**

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### **Expertise**

Maureen joined Segal Marco Advisors in 2011 and currently serves as Vice President, Corporate Governance Director where she leads corporate engagements on behalf of Segal Marco's clients and analyzes proxy voting issues. Maureen's work in shareholder advocacy began in 2003 as a Research Analyst for the Investor Responsibility Research Center. Since then she has specialized in engaging companies on behalf of investors. Prior to Segal Marco, Maureen was Head of Engagement at Conflict Risk Network, where she held dialogues with companies operating in Sudan and other conflict zones.

Maureen served on the Council of Institutional Investors Corporate Governance Advisory Council from 2015 to 2018. In 2020, she was elected Chair of the Governance Committee of the Board of Women Investment Professionals.

### **Education/Professional Designations**

Maureen received her M.A. from American University in Washington, D.C. and her B.A. from the University of Missouri-Columbia.



## **Anh Cao**

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### **Expertise**

Anh is a corporate governance analyst at Segal Marco Advisors. Anh started at the firm in 2016. At Segal Marco, she researches and supports matters for engagement with companies on corporate governance issues. Anh also supports with analyzing and voting proxy ballots for domestic and foreign markets.

### **Education/Professional Designations**

Anh obtained a Bachelor of Science from Northwestern University, with a major in Organization Behavior with a concentration in Mathematics.





# I. The Market Environment For Corporate Governance

## SEC Dampens Shareholder Rights

The regulatory landscape for corporate governance, environmental and social issues took sharp turns in 2019. Following failed attempts to move legislation through Congress and an inconsequential interpretative bulletin from the Department of Labor, opponents of shareholder rights found a willing Securities and Exchange Commission (SEC) to propose chilling changes to proxy voting and shareholder advocacy rules.

Segal Marco and the Council of Institutional Investors, as well as dozens of investors that have submitted public comment letters to the SEC are of the opinion that the proposed rules weaken shareholder rights. The SEC intends to finalize the rules in April 2020. The proposed version of the rules were approved in a 3–2 vote by the five Commissioners, with Chairman Jay Clayton and Commissioners Hester Peirce and Elad Roisman in support and Robert Jackson and Allison Lee dissenting.

Segal Marco's view is that the proposed rules are unnecessary and will hamper objective proxy voting research and weaken investors' ability to exercise their ownership rights by filing shareholder proposals. Segal Marco's full comment on the rules will be available on the SEC website prior to the close of the comment period on February 3, 2020.



## Summary of the SEC's Proposed Changes

### 1. Shareholder Advocacy Rule Summary

The proposed rules would add more procedural requirements and would make it more difficult for investors to submit resolutions to companies on governance issues.

Specifically, the requirements would:

- Replace the requirement that shareholders need to hold \$2,000 worth of stock for one year to be eligible to file a shareholder proposal to one of three options for eligibility. Those three options would be (1) \$2,000 worth of stock held for three years; (2) \$15,000 worth of stock for at least two years; or (3) \$25,000 worth of stock held for one year.
- Require additional documentation to be provided when a proposal is submitted on behalf of a shareholder-proponent.
- Require shareholder proponents to give dates and times when they could meet with the company rather than allowing investors and companies to convene their own meeting times.
- Prohibit a representative from participating in more than one proposal for the same shareholders' meeting.
- Require investors obtain higher levels of support to refile a proposal after the first year.

### 2. Proxy Advisor Rules Summary

The SEC is proposing amendments to its rules that would consider proxy voting advice as a solicitation and, therefore, subject to liability charges from the corporations covered by the research. The proposed amendments would condition the availability of certain existing exemptions from the solicitation provisions upon compliance with additional disclosures and procedural requirements. For example, proxy advisors would have to share their research with companies twice prior to publication and, if requested, include a hyperlink to a company's critique of the research.





## SEC Declines to Play Referee

Perhaps the most surprising development in SEC oversight of the shareholder engagement process was the Commission's quiet announcement on its website in September that it may choose to remove itself as the arbiter of which shareholder proposals merit inclusion in proxy statements.

The SEC announced it may decline to weigh in on the request for no-action process where companies argue shareholder proposals may be omitted and investors argue for their inclusion. Up until this point, the SEC reviewed both perspectives and offered its guidance on which party it found most persuasive. The September announcement made clear the SEC staff will "inform the proponent and the company of its position, which may be that the staff concurs, disagrees or declines to state a view, with respect to the company's asserted basis for exclusion." The Commission noted that its staff may respond orally rather than drafting a publicly available document. Historically, shareholders have been able to review previous no-action challenges when drafting proposals. Companies as well as research providers were able to collect information on how the SEC views a particular argument. Oral decisions lack transparency to market participants not directly involved in any specific no-action petition. Companies and shareholder proponents may take the matter to court but the costs can make the legal route prohibitive.

## Staff Legal Bulletin No. 14K

In October, the SEC issued Staff Legal Bulletin No. 14K to provide guidance on exclusions under the ordinary business rule that enables companies to omit certain shareholder proposals. The Commission signaled it was more amenable to excluding proposals where a company successfully made the case that the subject matter of the proposal is not a significant matter or where the scope and application of the proposal micromanaged how the firm handled the matter, even if considered significant.

Rule 14a-8(i)(7) establishes the threshold between ordinary business and a significant policy issue. Under the Rule, the Commission has long held shareholders may submit proposals on a significant policy issue that transcends day-to-day business matters, which has historically included issues such as executive compensation, climate change and political spending. With Bulletin No. 14K, the SEC narrowed the range of permissible proposals by redefining what constitutes a significant policy issue. The Commission outlined two new considerations for evaluating significance: (1) a company-specific view rather than a categorical determination on the subject matter (i.e., climate change); and (2) the delta between the proposal's request and the actions the company has already taken.

The Commission urged companies that are submitting no-action requests to provide a board analysis of whether a particular policy issue is significant to the particular firm based on specific substantive factors. The Commission also signaled that companies could make the argument that prior company actions on the issue could diminish the significance of the policy issue to the point where it is no longer significant to the company.



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The Commission also provided a new perspective on no-action arguments under the micromanagement grounds. The Bulletin reported, “two proposals focusing on the same subject matter may warrant different outcomes based solely on the level of prescriptiveness with which the proposals approach that subject matter.” Prescriptiveness is loosely defined in the Bulletin as imposing a specific strategy, method, action, outcome or timeline. The Commission appears to prefer proposals that raise an issue and leave it to the judgment of management and the board on how best to handle the response.

The Commission also encouraged shareholders to use sample language provided in an earlier bulletin (SLB No. 14F) when providing proof of ownership letters while making clear that mimicked language is not required.

## SEC Turns Focus to ESG Funds

In December, the Commission sent examination letters to money managers that offer environmental, social and governance (ESG) funds. Hester Peirce, one of the three SEC Commissioners to vote for the proposed rules on proxy voting and shareholder advocacy, has spoken publicly about her skepticism of ESG investing. “Having corporations accountable to one group, and that is shareholders, is a really valuable way to make sure they are doing the most that they can do for society. I don’t think trying to give corporations and their managers multiple targets to multiple audiences to please is really a very wise idea,” she said, according to CNBC. The Wall Street Journal reported that the letters requested data, such as a list of recommended stocks, models for assessing ESG performance and proxy-voting records. It is not yet clear whether or how the SEC will use the information collected as a result of the examination letters.

## ESG Growth Gains Steam

Despite Commissioner Peirce’s view, corporations appear to be headed in the opposite direction. In August, 181 CEOs signed onto a missive from the Business Roundtable that changed the business group’s statement on the purpose of a corporation. Since 1997 the Roundtable endorsed the principle of shareholder primacy, meaning the sole purpose of a corporation is to serve shareholders. The new statement broadens the stakeholder group that a corporation serves. It commits the CEOs of Amazon, Blackrock, Exxon Mobil and Wal-Mart among many other leading U.S. publicly traded firms to:

- delivering value to customers;
- investing in employees;
- dealing fairly and ethically with suppliers;
- supporting communities; and
- generating long-term value for shareholders.

Even traditional earnings calls are incorporating more time for ESG. Twice as many companies in the S&P 500® discussed ESG on their earnings calls in the third quarter of 2019 compared to the second quarter, according to The Wall Street Journal.

The perspective of the multi-stakeholder view on corporate purpose may be a reaction to consumer demand. A 2019 joint study on sustainability by the United Nations Global Compact and Accenture Strategy, The Decade to Deliver: A Call to Business Action, found 99 percent of surveyed CEOs from companies with more than \$1 billion in annual revenue believe sustainability will be important to their businesses’ future success.

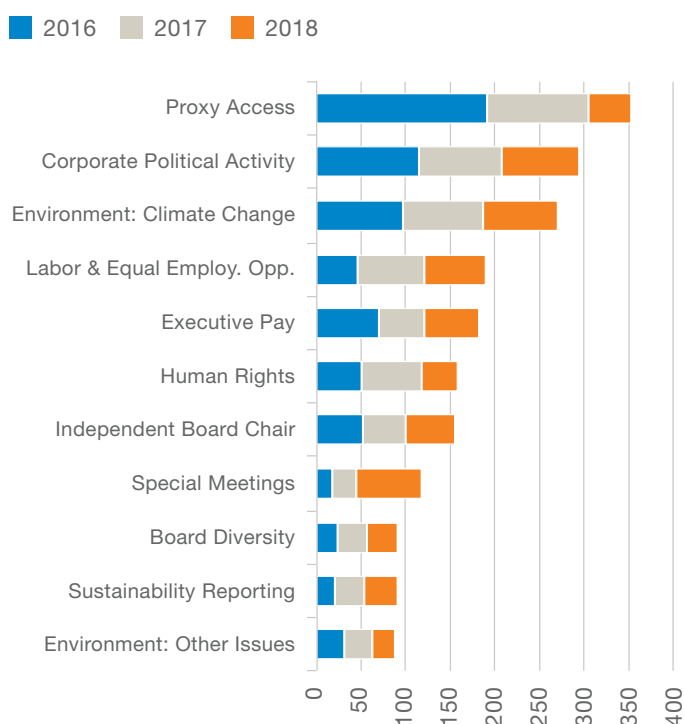




The top dozen investment consulting firms have integrated ESG into their manager research processes through ratings and expanded data collection, according to reporting by FundFire.

Companies are joined by audit firms, money managers, investors and consulting firms in their investigations of the ESG space. In November, the American Institute of Certified Public Accountants proposed rules that would allow auditors to measure ESG factors even where companies have not yet provided the data. The company would need to request the auditor perform an assessment of ESG factors to trigger the examination, according to *The Wall Street Journal*. The most recent [Trends Report](#) by the Social Investment Forum (SIF) found asset managers consider ESG criteria across \$11.6 trillion in assets, up 44 percent from \$8.1 trillion (see Table 2) in 2016. Investment consultants are delving into the space as well. The top dozen investment consulting firms have integrated ESG into their manager research processes through ratings and expanded data collection, according to reporting by FundFire. Investors interested in ESG have approached it through proxy voting, shareholder advocacy, asset allocation to ESG products and inquiries to money managers on ESG factors. As provided in Table 1, SIF reported the three most common subjects of shareholder proposals between 2016 and 2018 are: proxy access, corporate political activity, and climate change.

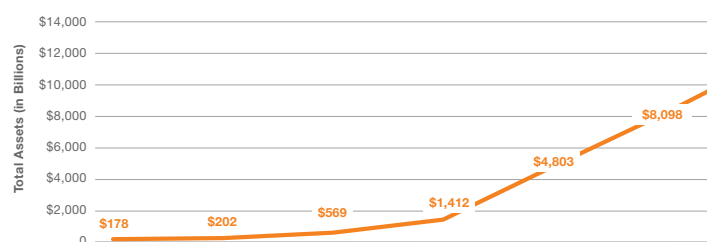
Table 1: ESG Shareholder Proposals



Source: U.S. Social Investment Forum, 2018 Report on U.S. Sustainable, Responsible and Impact Investing Trends

Table 2: ESG Growth

### Growth of ESG Incorporation by Money Managers 2005-2018



Source: U.S. Social Investment Forum, 2018 Report on U.S. Sustainable, Responsible and Impact Investing Trends



One negative consequence of SEC regulations that would weaken informed proxy voting and investors' ability to submit proposals is that such proposals help define the scope of ESG. Shareholders petition companies on a host of factors and investors vote on them, which provides companies with an indication of the factors that most resonate with their owners. There is no universal definition of ESG but the subject matter of shareholder proposals in any given year helps demarcate the territory.

Meanwhile, other markets are also trying to bring definition to the ESG space. The [U.K. Stewardship Code 2020](#) published by the Financial Reporting Council will include a stronger focus on ESG issues. The signatories of the U.K. Stewardship Code 2020 are expected to take into account how they monitor ESG factors, including climate change, and show how they are demonstrating their commitment.

## 2019 Investor Initiatives on ESG

Segal Marco clients joined other investors in several areas on their shareholder advocacy work in 2019. Investors frustrated with the growth of dual-class stock companies sought new avenues to try to encourage equal voting rights and to strengthen and promote shareholder rights. In addition to governance, the priority issues in 2019 were board diversity, pay parity, sexual harassment, opioids, executive compensation, human capital management (HCM) and the environment.

## Environmental Issues

Investors are eager for companies—particularly in the oil and gas sector—to report on sustainability efforts and forward-looking strategy that accounts for climate change. In 2017, proposals asking Exxon Mobil and Occidental Petroleum to provide detailed analyses of the risks posed to their business by climate change policies received majority votes from shareholders for the first time. The majority vote outcomes compelled both firms to report, although investors continue to push for more thorough disclosure. The New York Attorney General's (AG) office filed a lawsuit against Exxon Mobil in 2018 on the grounds that the company deceived investors about the risks posed by climate change regulation. In Oct. 2019, the New York court found the AG failed to prove the company made material misstatements or omissions to investors. Investors filed 32 proposals on environmental issues in 2019, spanning topics such as methane leaks, greenhouse gas goals, packaging, water conservation and pollution, deforestation, food waste and pesticides.



**“The time will come when there will be a threshold question that consumers will ask which is ‘can I trust this brand?’, and if the answer is ‘no’ they won’t buy anything. It will become a binary question.”**

*—Bruce Cleaver, CEO, DeBeers Group*

SOURCE: United National Global Compact and Accenture. 2019 CEO Study on Sustainability, The Decade to Deliver: A Call to Business Action.

One environmental issue that seems to have strong consensus among companies and investors is sustainability reporting. Research firm Si2 reported in 2018 that 78 percent of S&P 500 firms issue sustainability reports, although comparability is problematic given the customized nature of the information shared. The Office of the Illinois State Treasurer successfully engaged with four companies in 2019 that agreed to issue or enhance their annual reporting on sustainability efforts. O'Reilly Automotive and Crown Castle International published their first reports in December, while reports from Activision Blizzard and Intuitive Surgical are forthcoming.