Taking flight

Environmental sustainability proposals gain more attention

Building a better working world

Most sustainability disclosure is voluntary, and the most effective disclosure is company-specific — often determined with investor input.

Environmental sustainability proposals gain more attention

Shareholder-sponsored proposals on environmental sustainability are becoming more prevalent. Institutional investors are increasingly working to better understand the potential financial impact of sustainability issues on companies in their portfolios. By submitting and voting in favor of shareholders' environmental proposals and engaging on the topic, investors are calling for greater company attention to such areas as climate change and sustainability, energy and energy extraction-related risks (e.g., coal combustion, hydraulic fracturing), energy efficiency, recycling and environmental hazards in the air, water and soil. Investors play an important role in environmental and social (E+S) topics by drawing attention to the topic and influencing disclosure.

At the same time, more companies are putting greater effort into the disclosure of material E+S impact data, which some sustainability specialists may refer to more broadly as environmental, social and governance (ESG) or corporate social responsibility (CSR) data. While some companies are just now starting to discuss and measure sustainability impacts, other companies — mainly, the larger companies that have long issued sustainability reports — are continuing to enhance existing monitoring, reporting and related risk management processes. In addition, some of the largest companies are now focusing more closely on monitoring and reporting in connection with the global supply chain.

This publication looks at developments in the 2013 season — in particular, what companies are doing in the area of environmental sustainability. The report is based on the EY Corporate Governance Center's proprietary database and a review of more than 900 shareholder proposals submitted at Russell 3000 companies for annual meetings through 30 June 2013.[1]

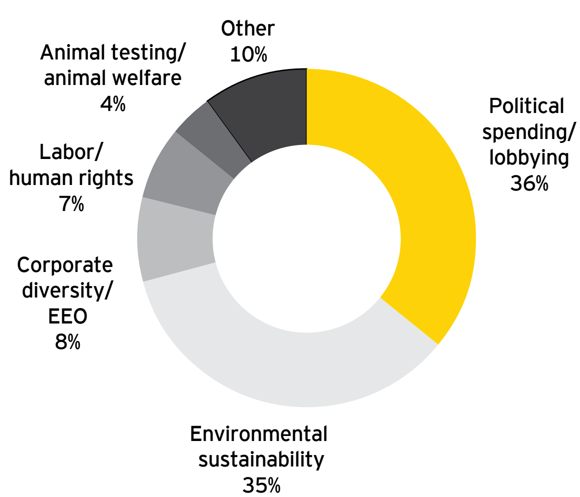
1. Vote results are calculated based on votes cast for and against the proposal. Previous-year data is full year unless otherwise stated.

E+S topics dominate the shareholder proposal landscape

This proxy season, shareholder proposal submissions across all topics grew by more than 6% over the same period last year. E+S proposals comprised the largest category of all shareholder proposals filed, at just under 40% of the total. [2]

- Within this category, two types of E+S proposals accounted for about 70% of submitted proposals: 1) proposals seeking enhanced disclosure on and board oversight of corporate political spending/lobbying, which represented 36% of E+S proposals, and 2) proposals seeking enhanced disclosure and greater company action on environmental sustainability, through the reduction of greenhouse gas (GHG) emissions, for example, which comprised 35% of the proposals.

Top E+S proposal topic areas



E+S proposals also represented the largest category of shareholder proposals voted – at more than a third of the total. Average support for E+S proposals stands at about 20%, which is twice the 2005 level of voting support. In addition, a growing number of these proposals is reaching the threshold level of 30% support, the level at which many boards take note of the proposals.

Voting support for environmental and social shareholder proposals by threshold

Summary data	2008	2009	2010	2011	2012	2013
More than 30% support	15%	18%	27%	31%	23%	30%
More than 20% support	30%	38%	44%	52%	45%	54%
More than 10% support	40%	48%	52%	59%	62%	65%
Total average support	14%	17%	18%	21%	19%	21%

The E+S category also has the highest percentage of shareholder proposals that are withdrawn in connection with engagement. As companies and investors pursue dialogue on E+S topics, shareholder proposals may be withdrawn due to an increased level of mutual understanding and/or specific action taken by the company.[3] In the past two years, roughly one-third of E+S proposals were withdrawn in connection with dialogue or action. In comparison, less than a quarter of all shareholder proposals were withdrawn in connection with dialogue or action.

- E+S proposals are ripe for engagement and successful withdrawal agreements, partly because many of them call for increased disclosure. Boards are increasingly willing to provide it as they begin to recognize the market value in creating transparency and accountability.

2. Other major proposal categories are board-focused, compensation and anti-takeover/strategic proposals.

3. Alternate reasons for withdrawals are technical, i.e., cases where the proposal or proposal sponsor failed to meet requirements for the inclusion of the proposal in a company's proxy materials.

All shareholder proposals

- Average support 33%
- Percentage of all shareholder proposal withdrawals via dialogue/action 24%

Environmental and social proposals

- Average support 21%
- Portion of all shareholder proposals submitted 38%
- Percentage of E+S proposal withdrawals via dialogue/action 30%

Environmental sustainability proposals

- Average support 23%
- Portion of all shareholder proposals submitted 13%; portion of E+S proposals submitted 35%
- Percentage of environmental sustainability proposal withdrawals via dialogue/action 43%

Climate change/sustainability proposals tend to be strongly supported and are one of the E+S proposal topics most likely to be withdrawn following company-investor dialogue and/or company action.

Climate change/sustainability a key component of the environmental category

A breakdown of E+S proposals shows that environmental proposals average slightly higher voting support than social proposals (23% versus 21%) and about twice the level of proposal withdrawals in connection with dialogue or action (at more than 40%).

These average support and proposal withdrawal figures appear to be driven in large part by proposals on climate change/sustainability, which seek enhanced sustainability-related disclosure and cuts in GHG emissions. Climate change/sustainability proposals account for nearly half of the environmental proposals submitted. In comparison, the next two largest categories of environmental proposals – energy efficiency/recycling and energy extraction-related risks – accounted for 14% and 12%, respectively, of the total.

- Average voting support for climate change/sustainability proposals stands at 27% this year, about a nine percentage point increase from 2005.
- A review of withdrawn climate change/sustainability shareholder proposals shows that the majority of the withdrawals were made in connection with dialogue or action. Nearly two dozen companies in more than a dozen industry sectors, spanning small- to large-cap companies, agreed to engage in robust dialogue and/or enhance sustainability reporting. Six of these companies committed to work with key suppliers to issue sustainability reports including on worker safety.[4]
- As more companies agree to rigorous sustainability reporting and climate change/sustainability proposals continue to receive high levels of support, it is likely that the pressure on those companies with less comprehensive and detailed reporting will grow.

4. *Investors Achieve Strong Results on Climate Change, Supply Chains, Water Risks During 2013 Proxy Season*, Ceres, 8 Aug 2013

The "ask" in climate change/ sustainability proposals

These shareholder proposals tend to request one of following:

- Enhanced sustainability disclosure — Shareholders request that the board prepare and/or make available to shareholders a sustainability report addressing GHG emissions (targets and goals), water conservation, waste minimization, energy efficiency and other E+S impacts. The report should address sustainability in operations and maintenance as well as design, and include a review of the company's E+S policies, practices and goals, as well as multiple objective statistical indicators relating to the above E+S impacts.
- Greater supply chain transparency — Shareholders request that the board take the steps necessary to require each of the company's significant suppliers (defined as those from which the company expects to purchase at least US$1 million in goods and services annually) to publish an annual, independently verifiable, sustainability report to be made available to its shareholders, including disclosures on the suppliers' objective assessments and measurements of performance on workplace safety, human and worker rights and environmental compliance, using internationally recognized standards, indicators and measurement protocols. The reports should also include incidents of non-compliance, actions taken to remedy those incidents and measures taken to contribute to long-term prevention and mitigation.
- Cuts in GHG emissions — Shareholders request that the board adopt quantitative goals, based on current technologies, for reducing total GHG emissions from the company's products and operations and that the company report to shareholders on its plans to achieve these goals.

Three largest environmental sustainability topics

1

Climate change/sustainability

- Portion of environmental sustainability proposals submitted 46%
- Average support 27%
- Percentage of withdrawals via dialogue/action 38%

2

Energy efficiency/recycling

- Portion of environmental sustainability proposals submitted 14%
- Average support 11%
- Percentage of withdrawals via dialogue/action 47%

3

Energy extraction risks

- Portion of environmental sustainability proposals submitted 12%
- Average support 27%
- Percentage of withdrawals via dialogue/action 50%

Leading company actions on environmental sustainability

In the supporting statement of a shareholder proposal, it is common for the proponent to reference the practices of a set of companies in order to create a point of comparison and demonstrate that the requested disclosures and actions are achievable. These references also serve, in effect, to communicate the proponent's ideas of leading practices in a particular area. For climate change/sustainability proposals, the predominant filers – public pension and socially responsible investment (SRI) funds — include some of these references:

- Nearly 80% of Fortune Global 500 companies are producing sustainability reports – with more than three-quarters of them providing disclosures based on Global Reporting Initiative (GRI) Guidelines.
- About 45% of S&P 500 companies are producing sustainability reports.
- Companies in the information technology and diversified industrial product sectors are using programs that require suppliers to track and report on key E+S factors.
- Retail and wholesale companies are publishing sustainability policies and reports that describe vendor standards and sustainable business practices; one proponent also highlighted a company that developed the auditing protocol for strengthening the voluntary program.
- Automotive companies are using ESG performance information in supplier selection programs.

Other examples of instances in which shareholder proponents have highlighted disclosure practices and related actions on environmental matters include:

- Oil and gas companies using quantitative performance metrics to better manage the environmental and community impacts of hydraulic fracturing (fracking) operations and publicly disclosing their progress
- Consumer product companies pursuing a policy of extended producer responsibility for post-consumer product packaging as a way to increase packaging recycling, reducing emissions and air and water pollution – and disclosing progress in these areas

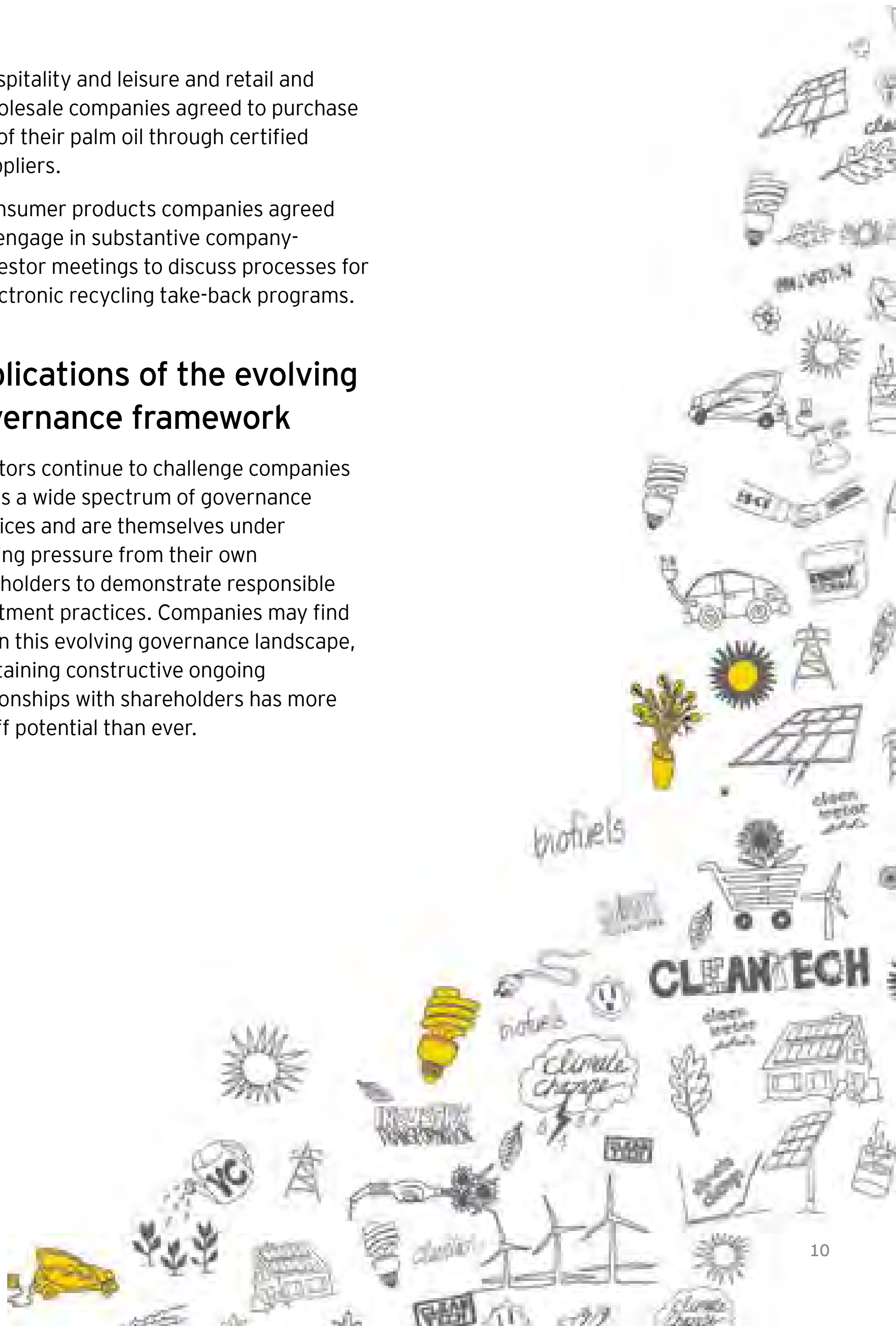
Company actions that led to proposal withdrawals

A significant portion of environmental proposals do not reach a shareholder vote as a result of robust dialogue and/or company action. Examples of cases in which this occurred in 2013 include:

- Four companies spanning three industries agreed to board level oversight of E+S matters.
- A financial institution agreed to develop a public E+S risk assessment policy that discusses how the company will address greenhouse gas emissions related to its lending and financing portfolios.
- Companies with fracking operations agreed to provide more disclosure with respect to specific actions that the company is taking to use less toxic substances in its fracking fluid, as well as providing information on how the company is ensuring that these efforts are carried out.
- Hospitality and leisure and retail and wholesale companies agreed to purchase all of their palm oil through certified suppliers.
- Consumer products companies agreed to engage in substantive company-investor meetings to discuss processes for electronic recycling take-back programs.

Implications of the evolving governance framework

Investors continue to challenge companies across a wide spectrum of governance practices and are themselves under growing pressure from their own stakeholders to demonstrate responsible investment practices. Companies may find that in this evolving governance landscape, maintaining constructive ongoing relationships with shareholders has more payoff potential than ever.



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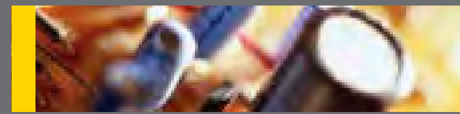

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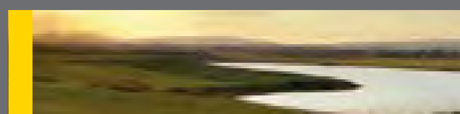

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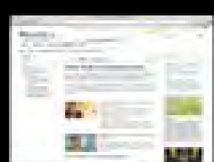

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