2022 Annual Review

UTAM
Engagement Highlights

UNIVERSITY OF TORONTO
ASSET MANAGEMENT CORPORATION

Federated Hermes
EOS

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When the University of Toronto announced climate-related targets for its long-term endowment portfolio in 2021, UTAM's next step was to translate that commitment into action. Within a year of the announcement, we have made considerable progress including reducing exposure to fossil fuel companies, allocating capital to new sustainability-focused managers and setting a new, ambitious carbon footprint reduction target.

Engagement – with our investment managers as well as companies we invest in – remains a key pillar of our approach to responsible investing. By representing our concerns clearly and consistently, we foster positive action and accountability on environmental, social and governance matters, including those affecting risk management, ongoing operations and long-term performance.

We value the efficiency and effectiveness of working collaboratively with other investors and with our engagement partners. EOS plays a key role in our engagement strategy, which amplifies UTAM's voice globally, leveraging the influence of a large asset base to make steady progress on priorities that align with our own. We are pleased to see that EOS continues to make progress towards its engagement targets.

Chuck O'Reilly
President and Chief Investment Officer,
University of Toronto Asset Management Corporation

UTAM's activity for 2022

Engagement by region

In 2022, we engaged with 827 companies on 3,362 environmental, social, governance, strategy, risk and communication issues and objectives. Our holistic approach to engagement means that we typically engage with companies on more than one topic simultaneously.

We engaged with 827 companies over the last year.

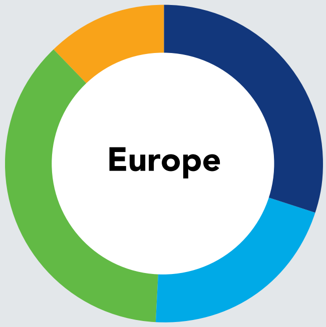
- Environmental **29.0%**
- Social and Ethical **22.7%**
- Governance **36.1%**
- Strategy, Risk and Communication **12.1%**

We engaged with 79 companies over the last year.

- Environmental **29.9%**
- Social and Ethical **20.4%**
- Governance **38.3%**
- Strategy, Risk and Communication **11.5%**

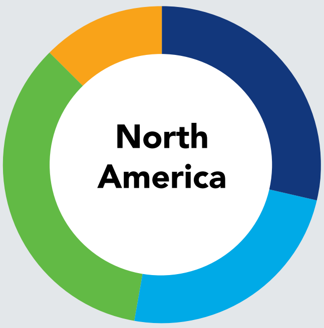
We engaged with 106 companies over the last year.

- Environmental **28.7%**
- Social and Ethical **22.2%**
- Governance **35.3%**
- Strategy, Risk and Communication **13.8%**



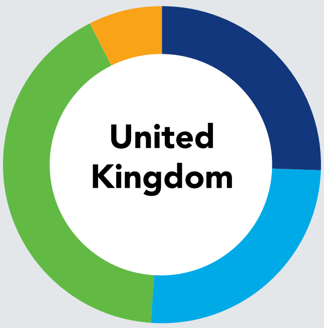
We engaged with 168 companies over the last year.

- Environmental **30.1%**
- Social and Ethical **21.0%**
- Governance **36.8%**
- Strategy, Risk and Communication **12.1%**



We engaged with 387 companies over the last year.

- Environmental **28.9%**
- Social and Ethical **24.0%**
- Governance **34.7%**
- Strategy, Risk and Communication **12.5%**



We engaged with 62 companies over the last year.

- Environmental **25.8%**
- Social and Ethical **25.4%**
- Governance **41.3%**
- Strategy, Risk and Communication **7.5%**

We engaged with 25 companies over the last year.

- Environmental **27.4%**
- Social and Ethical **19.1%**
- Governance **40.5%**
- Strategy, Risk and Communication **13.1%**

Engagement by theme

A summary of the 3,362 issues and objectives on which we engaged with companies in 2022 is shown below.

Environmental topics featured in 29.0% of our engagements over the last year.

- Climate Change **75.9%**
- Forestry and Land Use **6.9%**
- Pollution and Waste Management **11.7%**
- Supply Chain Management **2.3%**
- Water **3.3%**

Social and Ethical topics featured in 22.7% of our engagements over the last year.

- Bribery and Corruption **1.4%**
- Conduct and Culture **9.9%**
- Diversity **19.0%**
- Human Capital Management **22.4%**
- Human Rights **40.8%**
- Labour Rights **5.6%**
- Tax **0.8%**

Governance topics featured in 36.1% of our engagements over the last year.

- Board Diversity, Skills and Experience **24.4%**
- Board Independence **13.3%**
- Executive Remuneration **45.5%**
- Shareholder Protection and Rights **14.5%**
- Succession Planning **2.3%**

Strategy, Risk and Communication topics featured in 12.1% of our engagements over the last year.

- Audit and Accounting **13.5%**
- Business Strategy **31.1%**
- Cyber Security **2.2%**
- Integrated Reporting and Other Disclosure **24.3%**
- Risk Management **28.9%**

Engagement methodology and progress in 2022

Our proprietary milestone system allows us to track progress in our engagements relative to the objectives set at the beginning of our interactions with companies. The specific milestones used to measure progress in an engagement vary depending on each concern and its related objective. They can broadly be defined as follows:

- **Milestone 1** Concern raised with the company at the appropriate level
- **Milestone 2** The company acknowledges the issue as a serious investor concern
- **Milestone 3** Development of a credible strategy/Stretching targets set to address the concern
- **Milestone 4** Implementation of a strategy or measures to address the concern

Milestone stage of engagement

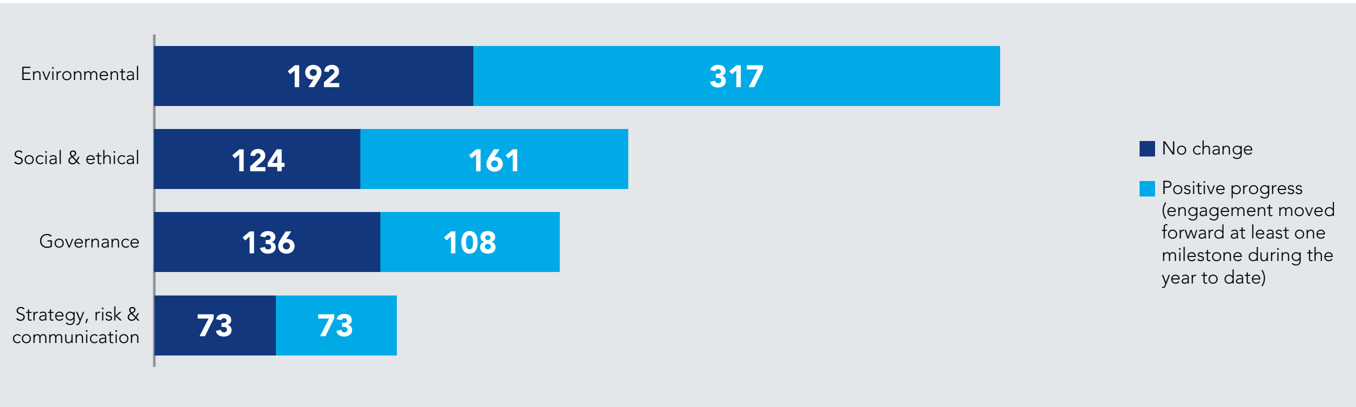
The chart below shows the milestone stage of our engagement objectives by theme.

Theme	Total Engagement Objectives*	Engagement objective stage (last milestone completed)			Closed engagement objectives	
		Milestone 1	Milestone 2	Milestone 3	Completed	Discontinued
Environmental	509	125	185	113	71	15
Social and ethical	285	60	113	50	45	17
Governance	244	52	73	46	41	32
Strategy, risk and communication	146	21	53	35	25	12
Total engagements	**1,184**	**258**	**424**	**244**	**182**	**76**

*Includes objectives which were live in the period. Objectives are live when Milestone 1 has been completed.

Engagement progress in 2022

We made solid progress in delivering engagement objectives across regions and themes. At least one milestone was moved forward for about **56%** of our objectives during the year. The following chart describes how much progress has been made in achieving the milestones set for each engagement.



Supporting the UN Sustainable Development Goals

The chart below illustrates the number of engagement objectives and issues on which we have engaged in the last year, which we believe are directly linked to an SDG (noting that one objective or issue may directly link to more than one SDG).

Proportion of issues and objectives engaged in 2022 linking to the SDGs

SDG		SDG		SDG	
13 Climate action	36%	16 Peace, justice & strong institutions	9%	1 No poverty	3%
12 Responsible consumption and production	27%	3 Good health and well-being	9%	6 Clean water and sanitation	3%
8 Decent work and economic growth	16%	9 Industry, innovation and infrastructure	8%	4 Quality education	1%
10 Reduced inequality	16%	15 Life on land	5%	2 Zero hunger	1%
5 Gender equality	16%	14 Life below water	3%	17 Partnerships to achieve the goal	1%
7 Affordable and clean energy	11%	11 Sustainable cities and communities	4%		

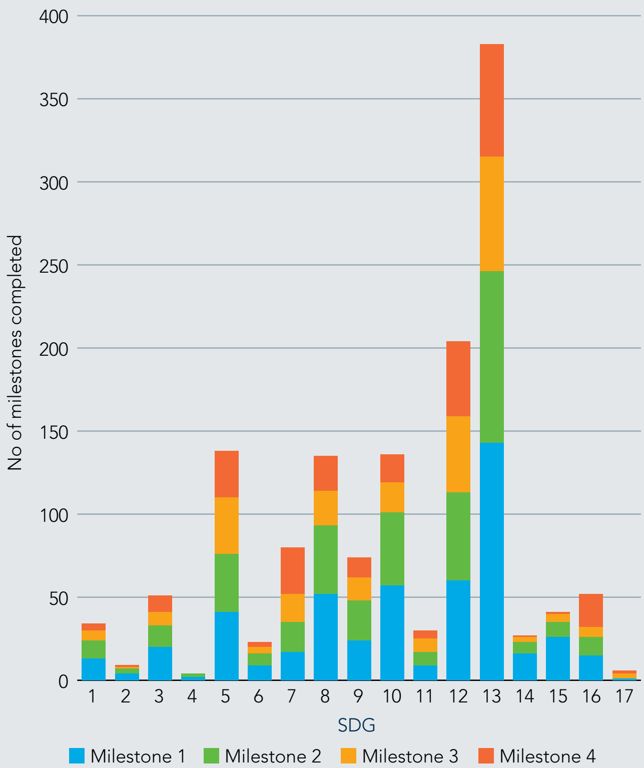
2,035 of the issues and objectives engaged in 2022 were linked to one or more of the SDGs

Why engage on the SDGs?

Investors and their representatives play a key role in supporting the delivery of the UN SDGs. This could be by creating positive outcomes for society through investments and engagement as the goals recognise the role of the private sector in financing sustainable development. Moreover, the SDGs provide a common framework and language for investors and companies to work towards the achievement of the shared goals, with measurable indicators of progress. They also provide a clear time frame in which change needs to take place, helping to set targets and create a greater sense of urgency, while considering what action is needed from business to achieve sustainable development, beyond the typical incremental improvements and business-as-usual targets.

Our engagement with companies encourages them to act responsibly and reduce their negative impacts on society, across their value chains. We are also suggesting changes that could provide a positive impact. Our view is that the long-term success of business is inextricably linked to achievement of the goals because the SDGs help to create an economic context and society in which businesses can best thrive.

Milestone progress of SDG-linked engagement objectives



Source: EOS data for 2022

The EOS approach to engagement

EOS at Federated Hermes is a leading stewardship service provider. Our engagement activities enable long-term institutional investors to be more active owners of their assets, through dialogue with companies on environmental, social and governance issues.

We believe this is essential to build a global financial system that delivers improved long-term returns for investors, as well as better, more sustainable outcomes for society.

> **Our Engagement Plan is client-led – we undertake a formal consultation process with multiple client touchpoints each year to ensure it is based on their long-term objectives, covering their highest priority topics.**

Our services

Engagement

We engage with companies that form part of the public equity and corporate fixed income holdings of our clients to seek positive change for our clients, the companies and the societies in which they operate.

Public policy

Engaging with legislators, regulators, industry bodies and other standard-setters to shape capital markets and the environment in which companies and investors can operate more sustainably.

Voting

We make recommendations that are, where practicable, engagement-led and involve communicating with company management and boards around the vote. This ensures that our rationale is understood by the company and that the recommendations are well-informed and lead to change where necessary.

Screening

We help our clients to fulfil their stewardship obligations by monitoring their portfolios to regularly identify companies that are in breach of, or near to breaching, international norms and conventions.

Advisory

We work with our clients to develop their responsible ownership policies, drawing on our extensive experience and expertise to advance their stewardship strategies.

The EOS advantage

- **Relationships and access** – Companies understand that EOS is working on behalf of pension funds and other large institutional investors, so it has significant leverage – representing assets under advice of over US$1.34tn as of 31 December 2022. The team's skills, experience, languages, connections and cultural understanding equip them with the gravitas and credibility to access and maintain constructive relationships with company boards.
- **Client focus** – EOS pools the priorities of like-minded investors, and through consultation and feedback, determines the priorities of its Engagement Plan.
- **Tailored engagement** – EOS develops engagement strategies specific to each company, informed by its deep understanding across sectors, themes and markets. It seeks to address the most material ESG risks and opportunities, through a long-term, constructive, objectives-driven and continuous dialogue at the board and senior executive level, which has proven to be effective over time.

Foreword

Leon Kamhi
Head of Responsibility and EOS

In 2022, a host of geopolitical and macroeconomic factors combined to threaten the fragile recovery from the pandemic. At the same time, record-breaking summer temperatures in Europe and devastating floods in Pakistan provided a sobering reminder of the human and financial cost of the climate crisis – and the fact that time is running out.

The adoption of the Kunming-Montreal Global Biodiversity Framework by almost 200 countries at the end of 2022 was one of the few bright spots in a turbulent year. Soaring inflation and the resulting cost of living crisis posed considerable challenges for companies, their employees, suppliers and customers, just as the global economy was beginning to emerge from the pandemic.

Acknowledging this, EOS integrated cost-of-living engagements into its wider stewardship programme. We asked companies to provide an assessment of the impacts on their business model and their stakeholders, and the actions they could take to help support the most affected, without damaging their long-term business objectives or fuelling inflation.

With food and fuel prices rising in the wake of Russia's invasion of Ukraine, there were fears that attempts to tackle the climate crisis would stall. Instead, the soaring price of fossil fuels reinforced the need for a low carbon transition and a faster switch to renewable energy. Encouragingly, we are now seeing some governments and companies recognising that demand reduction through the adoption of energy efficiency measures can play just as important a role as supply substitution.

Throughout 2022, we sought to engage companies on these challenges, without losing focus of the end goal – to limit global heating to a maximum of 1.5°C. We also continued our leading work on biodiversity, advocating for an ambitious Global Biodiversity Framework (GBF) ahead of COP 15. The GBF adopted in December features a target to protect at least 30% of land and seas by 2030 and addresses key issues related to biodiversity loss, such as subsidies and the financing gap.

Polarising landscape

We carried out our company engagements and public policy advocacy within a polarising landscape for active ownership and responsible investing. While some policymakers and investors pushed for a swifter transition to a low carbon economy, others concerned about changes to economic structures were stridently opposed to 'ESG', and climate action in particular.

It is odd that although ESG entered the investment industry's lexicon way back in 2006 with the launch of the Principles of Responsible Investment (PRI), it feels like it was never more misunderstood than in 2022. We saw how the weaponisation of ESG by both its promoters and detractors for commercial or political purposes reached new levels, and views on ESG became highly polarised. It is critical therefore that all in the investment industry, including EOS on behalf of its clients, remain focused on delivery in line with the long-term interests of the underlying beneficiaries.

Last year we also saw how well-intentioned regulators seeking to protect investors and get a grip on greenwashing added to the turmoil with unclear and burdensome requirements, which are unlikely to help develop a sustainable economy. We would rather see a greater focus on the role that stewardship plays in delivering sustainable outcomes and the enhancement of an investment's performance.

2023 may bring more of the same. Still, I hope that it will be a year in which investment and stewardship support the creation of wealth for investors – sustainably, and with a laser focus on their interests, undistracted by political aims or virtue signalling.

Our engagement plan

Our engagement plan identifies 12 key themes and 32 related sub-themes. We find this breadth of coverage is necessary to reflect the diversity of the issues affecting companies in our global engagement programme.

The war in Ukraine, the uneven global post-pandemic recovery and the increasing severity of extreme weather events linked to global warming contributed to an acute energy and cost of living crisis in 2022. Increasingly, employees found themselves disenfranchised and under daily pressure, while the risks of human rights violations worldwide intensified.

While COP27 on climate disappointed some, COP 15 on biodiversity delivered a Global Biodiversity Framework that was adopted by almost 200 countries. This included a target to protect at least 30% of land and seas by 2030 – a tacit recognition that the natural world is facing irreversible biodiversity loss through the impacts of climate change, land-use change and pollution. This turbulent geopolitical and economic landscape served to solidify our existing engagement priorities, while placing them in a new context.

The Global Biodiversity Framework includes a target to protect at least **30%** of land and seas by 2030.

Priority themes

In 2023, we will continue our focus on the most material drivers of long-term value, with our four priority themes:

Climate change action

The current energy trilemma – an overlap of accelerating climate change, challenges for energy security, and rising costs and inequality undermining energy affordability – is a potential risk to climate action in the short term. In the medium term, however, the trilemma may help to accelerate the transition away from fossil fuel resources.

Our engagement remains focused on companies having a strategy and greenhouse gas reduction targets aligned with the Paris Agreement, seeking to limit climate change to **1.5°C** together with aligned financial accounts and political lobbying.

Our engagement remains focused on companies having a strategy and greenhouse gas reduction targets aligned with the Paris Agreement, seeking to limit climate change to 1.5°C, together with aligned financial accounts and political lobbying. Under the broader Glasgow Financial Alliance for Net Zero, our own engagement-driven targets under the Net Zero Asset Managers initiative will intensify engagement with banks, ensuring that their net-zero ambitions are aligned with those of asset managers.

EOS will continue to lead or co-lead collaborative engagements across multiple sectors through the Climate Action 100+ and Institutional Investors Group on Climate Change (IIGCC) initiatives. We have started engaging more systematically on physical climate risk at exposed companies, targeting the development of adaptation plans that will bring much needed resilience. We will strengthen our focus on the need for a 'just transition' and address the human rights impacts of climate change.

Bruce Duguid
Head of Stewardship, EOS

Engagement themes for 2023-25

Human and labour rights

As we continue to engage on this enduring priority theme, we expect companies to acknowledge the likelihood that human rights impacts may be present within operations and supply chains, and to demonstrate appropriate board and executive-level governance of human rights. Our engagement focuses on ensuring that companies do not infringe upon basic human rights, and provide effective remedy in the case of any harm, while taking steps to provide fair and equitable access to finance, healthcare, and nutrition.

We will continue to focus on the protection of indigenous and community rights and human rights in high-risk regions such as disputed territories or areas of conflict. We will engage on the protection of digital rights in the virtual world, such as challenges to the right to data privacy, the right to freedom of expression, and protection from unfair biases arising from artificial intelligence.

We will also promote the corporate application of the UN Guiding Principles (UNGPs) on Business and Human Rights, for the next decade of their implementation.[1] We will focus on escalated breaches of the UN Global Compact principles for human rights including considering voting against directors if these breaches are not being adequately remediated or if the company lags on human rights benchmarks.

[1] OHCHR | UNGPs next 10 years project

We will continue our focus on diversity, equity, inclusion and representation, asking companies to develop a strategy to achieve proportionate ethnic and gender representation at all levels.

Human capital

In the wake of the 'great resignation' triggered by the pandemic, the increased interest in amplifying worker voice through collective bargaining, and the cost-of-living crisis, we are intensifying engagement across this theme. We would like companies to provide fair wages and benefits so all can afford a decent living standard. Companies should also develop and implement a human capital management strategy to promote best practice physical wellbeing (including health and safety) and mental wellbeing in the workplace.

We will also continue our focus on diversity, equity, inclusion and representation, asking companies to develop a strategy and action plan to close the ethnic pay gap and achieve proportionate ethnic and gender representation at all levels. We will challenge companies to expand their consideration of diversity metrics to include representation and equity for the LGBTQ+ community and people with disabilities. These strategies should include articulation of culture and employee proposition to improve workforce loyalty and wellbeing.

Board effectiveness

In 2023, to enhance the quality of board performance and corporate decision-making, we will focus on ensuring that boards make improvements to ethnic diversity that at least match the recent progress on gender diversity. The goal should be to achieve a representation that is reflective of the diversity of the stakeholders it aspires to serve.

We will also ask boards to demonstrate the lessons learned post-pandemic, including the possibility for more internationally-diverse board appointments, enabled by more effective remote working practices. We remain committed to improving a board's "software", which relates to how it functions, in addition to its "hardware", which relates to its composition and structure. The board should continuously monitor and assess the prevailing company culture to ensure it is in line with the company's purpose, strategy and values.

Expanding themes

In addition to the above priority themes, we will continue our engagement on these expanding topics:

Biodiversity

We will focus our engagement on halting and reversing marine and terrestrial biodiversity loss at companies that are involved in the production and selling of food. Other key challenges include antimicrobial resistance and deforestation. As we outlined in our white paper on biodiversity, published in February 2021,[2] companies must identify, assess and measure their impacts and dependencies on biodiversity and ecosystem services. They must reduce their impacts on biodiversity across the value chain following the mitigation hierarchy, and aim for a net-positive impact on biodiversity as best practice. Depending on the specific company context, engagement will cover issues including deforestation, water stress, regenerative agriculture, sustainable proteins and chemical runoff management.

[2] Our Commitment to Nature (hermes-investment.com)
[3] EOS Digital Rights Principles

Digital rights

We will engage companies on our Digital Rights Principles,[3] which we published in 2022. Digital products and services can play a critical role in strengthening human rights but have also brought unanticipated harms and new challenges. We engage companies on negative societal impacts including problematic content on social media, misuse of artificial intelligence, health and safety impacts on children and young people, environmental and social impacts in hardware supply chains, and the growing digital divide. We expect companies to balance freedom of expression with their obligations to remove problematic content and take action to respect privacy rights online.

Tax

Tax systems and revenue are vital to the functioning of wider societal services such as health, welfare, justice, emergency services, education and environmental protection. Public services are under tremendous strain in the wake of the pandemic and soaring inflation has only added to the pressure. Companies that seek to aggressively minimise their tax payments will face increasing legal, financial and reputational risks as regulation tightens.

Investors need sufficient information to gauge a company's tax position and governance approach and anticipate any future risks to their holdings. EOS will publish its Responsible Tax Principles in 2023 and our engagement expectations will focus on four critical areas: tax policy, governance, stakeholder engagement and transparency.

In addition to these priority and expanding themes, we will maintain our comprehensive engagement plan covering a broad range of other areas. These include seeking to avoid the emergence of 'superbugs' through antimicrobial resistance, increasing resource efficiency through the circular economy, reducing all forms of harmful pollution, and seeking positive wider societal outcomes through increased corporate responsibility.

A guide to engagement terminology

Our engagement approach is systematic and transparent. Our proprietary milestone system allows us to track the progress of our engagements relative to the objectives set for each company.

Objectives

We set clear and specific objectives within our company engagements to ensure we achieve positive outcomes. An objective is a specific, measurable change defined at the company – an outcome we are seeking to achieve. Each objective is tracked using milestones. Objectives are regularly reviewed until they are completed – when the company has demonstrably implemented the change requested – or discontinued. Objectives may be discontinued if the objective is no longer relevant, or because the engagement is no longer feasible or material.

We may engage with a company on multiple objectives at any one time, covering a variety of material ESG issues. An example of an objective could be: "Development of a strategy consistent with the goals of the Paris Agreement, including setting science-based emissions reduction targets for operating emissions (Scopes 1 and 2 emissions)." Each objective relates to a single theme and sub-theme.

> **To measure our progress and the achievement of engagement objectives, we use a four-stage milestone strategy.**

Issues

How does an objective differ from an issue, another term we use within our engagement? An issue is a topic we have raised with a company in engagement, but where we do not precisely define the outcome that we are seeking to achieve. This can be more appropriate if the issue is of lower materiality and so we do not anticipate engaging with the frequency required to pursue an objective. Or perhaps we are still in the process of identifying what type of change we may want to see at a company and so are not yet able to set a precise objective. Issues are frequently used for companies outside our continuous engagement programme, for example those where we typically engage only around the annual shareholder meeting and our voting recommendation.

Milestones

To measure our progress and the achievement of engagement objectives, we use a four-stage milestone strategy. When we set an objective at the start of an engagement, we will also identify recognisable milestones that need to be achieved. Progress against these objectives is assessed regularly and evaluated against the original engagement proposal.

Actions

These are the interactions that take place between our engagement professionals and the companies or public policy bodies with whom they are engaging. Every call, meeting or correspondence is recorded as an action. Actions can be linked to objectives or issues. We only consider companies to be engaged when we have an individual interaction with the company that relates to an objective or issue.

Environmental

Climate Action 100+ hits five-year mark

Climate Action 100+ has notched up five years of collaborative engagements with the world's biggest emitters and is now looking to its second phase. Owen Tutt reflects on the achievements to date and the challenges that lie ahead.

The turbulent economic and political environment of 2022 pushed climate change engagement into new territory. The fuel crisis, triggered in large part by the Russia-Ukraine conflict, put the energy transition under short-term strain with coal rebounding as a fuel of choice. But the long-term tailwinds propelling energy efficiency improvements and the competitiveness of renewables are expected to accelerate the transition over the longer term.

Governments called for increased oil and gas production as they scrambled to replace Russian gas with alternative supplies. Meanwhile, supply chain disruption and interest rate rises have challenged renewable energy producers, while some are exposed to windfall taxes meant to alleviate the cost of living crisis. Disappointingly, COP27 failed to secure an international agreement on fossil fuel phase-out or accelerated emissions reductions. Yet the US Inflation Reduction Act, Europe's REPowerEU plan, Japan's Green Transformation (GX) programme, and a new Brazilian government pledging action on deforestation all signal growing policy support for increased climate action and financial support for low-carbon technologies.

This all occurred in another year of climate extremes with a summer heatwave in Europe, extreme flooding in Pakistan and wildfires in the US. The key question is whether the short-term setbacks are small enough and the long-term tailwinds strong enough to keep the Paris Agreement's 1.5°C goal alive, thereby minimising the climate risk to investors and society as a whole. The UN's 2022 Emissions Gap Report found that this may still be possible, but the rate of decarbonisation must be truly transformative.

Given this, investor engagement on climate change is vital to help steward companies through a period of intense economic transformation. The collaborative engagement initiative Climate Action 100+ (CA100+) has been at the forefront of this activity for the last five years, and EOS has played an important role within it.

Since 2017 CA100+ has grown to include

Over
700 signatories

1.5°C

representing over
US$68tn
in assets under management

Source: CA100+

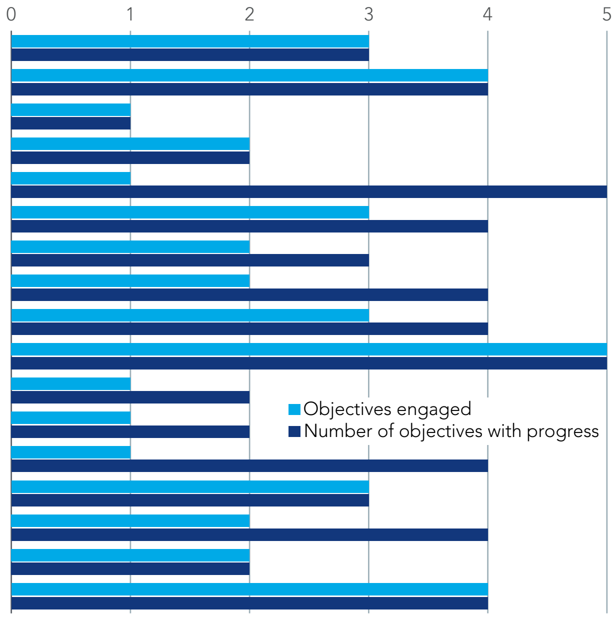
Progress made

Since 2017, CA100+ has grown to include 700 signatories representing over $68tn in assets under management – more than 50% of the global total. Since the initiative's inception, EOS has advised on high-level governance and engagement strategy, as well as leading or supporting a significant portion of company engagement dialogues. In 2022 we acted as lead or co-lead engager for 24 companies, although EOS and CA100+ paused engagement at three Russian companies after the start of the Russia-Ukraine conflict.

Owen Tutt
Theme co-lead: Climate Change

Progress of environmental objectives for selected CA100+ companies engaged by EOS, 2022

Company Name	EOS Sector	Participation
Mercedes-Benz Group	Automobiles	Lead
Bayerische Motoren Werke	Automobiles	Co-lead
Volkswagen	Automobiles	Co-lead
Dow	Chemicals	Co-lead
Walmart	Food, Beverages & Forestry	Co-lead
Hon Hai Precision Industry	Industrials	Co-lead
POSCO Holdings	Mining & Metals	Co-lead
BP	Oil & Gas	Co-lead
Chevron	Oil & Gas	Co-lead
Kinder Morgan	Oil & Gas	Co-lead
PetroChina	Oil & Gas	Co-lead
Petroleos Mexicanos	Oil & Gas	Co-lead
TotalEnergies	Oil & Gas	Co-lead
Enbridge	Oil & Gas	Support
AP Moller – Maersk	Transportation	Co-lead
Stellantis	Transportation	Co-lead
Lockheed Martin	Transportation	Support



Source: EOS data

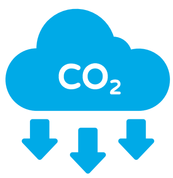
In October 2022, the CA100+ Net Zero Benchmark revealed the impressive progress to date with 75% of focus companies committing to achieving net-zero emissions by 2050 or sooner. Some 92% have disclosed that there is board oversight of climate change, and 91% have aligned their climate disclosures with the TCFD recommendations. Also, the electricity utility Enel became the first company to score positively on all nine currently-assessed benchmark indicators.

> **We made a statement at the AGM with other co-leads, supporting the company's efforts but also identifying areas where we expected to see further progress.**

However, companies still need to match their long-term ambitions with comprehensive 1.5°C-aligned short- and medium-term targets, and disclose credible strategies to achieve these. For example, only half of the CA100+ focus companies have net-zero targets that include material Scope 3 emissions, only half have disclosed decarbonisation strategies, and just 20% have medium-term targets that were assessed by CA100+ as aligned with 1.5°C. Also, only 23% of companies have committed to aligning their lobbying activities with the Paris Agreement, despite the importance of policy support for achieving company decarbonisation.

Only

23%



of companies have committed to aligning their lobbying activities with the Paris Agreement, despite the importance of policy support for achieving company decarbonisation.

Engaging for climate ambition

In 2022 we continued to push for progress where companies lagged best practice, as well as welcoming the setting of new targets by companies such as Danone. In December the French food company set Science-Based Targets initiative-validated 1.5°C -aligned emissions targets, which we have engaged on since 2019 as CA100+ lead.

Also in Europe, particularly at oil and gas companies, there was a surge in companies disclosing their climate transition plans and putting them to a vote at the annual shareholder meeting, sometimes referred to as a say-on-climate vote. These plans became an area of focus for CA100+ co-leads, requiring some intensive engagement to inform the analysis distributed to CA100+ signatories, and our vote recommendations to clients.

For example, at BP we met repeatedly with management, including the CEO, to challenge the strategy put forward. We also made a statement at the AGM with other co-leads, supporting the company's efforts but also identifying areas where we expected to see further progress. At TotalEnergies, we determined that the climate strategy remained materially below our sector-specific expectations, and escalated our concerns by pre-declaring our intention to recommend a vote against the climate change progress report. We also met with the CEO at the company's headquarters in Paris.

At UK energy utility Centrica, we led the CA100+ engagement on its climate transition plan ahead of the annual shareholder meeting. We recognised the significant progress made by the company in developing a strategy to reach net-zero emissions by 2045 for Scopes 1 and 2, and by 2050 for Scope 3. But we asked for greater detail on the strategy for heat energy decarbonisation and later raised this in board-level conversations.

COP26 in Glasgow in 2021 elevated awareness of the outsized impact of methane emissions on climate change, which provided a tailwind for our longstanding engagement on the issue.

The mining companies Anglo American and Rio Tinto, where we engage as part of the CA100+ group, also held say-on-climate votes in 2022. In engagement ahead of the votes, we welcomed the companies' improved targets for Scopes 1 and 2 emissions, which we assessed as substantially aligned with 1.5°C. We also discussed their distinct approaches to targeting Scope 3 reductions, with one opting for an emissions reduction target and the other a customer engagement target.

While say-on-climate votes were less common in North America, a flurry of climate-related shareholder proposals were filed at US and Canadian banks. These asked the banks to align their financing with the International Energy Agency's Net Zero by 2050 scenario, including by no longer financing new fossil fuel projects. We assessed these proposals on a case-by-case basis and supported those that were not overly prescriptive and aligned with an energy transition in line with 1.5°C, for example at Toronto-Dominion Bank and JPMorgan Chase.

In our role as CA100+ co-lead for the US oil company ConocoPhilips and in response to the board's failure to implement a 2021 shareholder proposal requesting absolute Scopes 1-3 emissions reduction targets, we filed an exempt solicitation. This publicly urged shareholders to vote against the chair of the board's sustainability and public policy committee.

COP26 in Glasgow in 2021 elevated awareness of the outsized impact of methane emissions on climate change, which provided a tailwind for our longstanding engagement on the issue (see Q&A on methane emissions). This was realised in a shareholder proposal filed at Chevron, where we also co-lead the CA100+ engagement, requesting a report on the company's methane emissions. We successfully urged the board to support this resolution, and filed an exempt solicitation encouraging investors to vote for the board's recommendation. The resolution ultimately passed with 98% support.


The mining companies Anglo American and Rio Tinto, where we engage as part of the CA100+ group, also held say-on-climate votes in 2022.


It is important for companies to develop strategies to reduce their emissions footprint, but they should also recognise where they are reliant on significant public policy and technology development.

A systemic risk requires systemic action

It is important for companies to develop strategies to reduce their emissions footprint, but they should also recognise where they are reliant on significant public policy and technology development. They must assess and disclose the financial consequences of the risks and opportunities that arise from their own climate-related actions and the systemic economic impacts of the energy transition and climate change. We are therefore increasingly scrutinising and engaging companies to ensure that corporate lobbying of policymakers helps rather than hinders the development of responsible climate policy, and that companies properly consider the financial impact of climate-related risks and opportunities in their accounts and audit process.

As CA100+ co-lead for the German automobile companies BMW, Mercedes-Benz and Volkswagen, in 2022 we intensified our engagement on aligning their public policy lobbying with their ambitions for achieving net-zero emissions. We specifically requested transparency on climate-related lobbying activities, which BMW and Mercedes provided through lobbying reports.

Volkswagen remained reluctant to do the same, so we escalated our engagement by supporting the filing of a shareholder resolution asking for an explanation of how its lobbying activities help to address climate risk. In response to the company's rejection of this resolution, we voiced our support for a group of investors taking legal action to challenge the decision. We also recommended voting against the discharge of the management and supervisory boards in connection to this issue, and other governance concerns.

As CA100+ co-lead for the German automobile companies BMW, Mercedes-Benz and Volkswagen, in 2022 we intensified our engagement on aligning their public policy lobbying with their ambitions for achieving net-zero emissions.

At Hon Hai Precision Industry (better known internationally as component supplier Foxconn) we welcomed the submission of its emissions reduction targets to the Science-Based Targets initiative. As CA100+ co-lead for the company, we pressed it to improve its climate risk disclosure and align these with the TCFD recommendations to give investors better visibility of its exposure to climate-related risk. This has also been an engagement priority at Hong Kong's Power Assets Holdings, where we are in the CA100+ support group, and have seen progress in 2022. In our CA100+ co-lead engagement with South Korea's Posco, we sought more granular disclosure of emissions to allow for a comprehensive assessment of the impacts of the conglomerate's distinct businesses.

And at CRH, a building materials company, we first requested in 2020 that the audit committee chair improve the consideration of climate-related risk in the company's financial accounts. In 2022, we met the board chair to communicate our concerns about the lack of progress on this aspect of the accounts and ultimately recommended a vote against the re-election of the audit committee chair.

Likewise, at Air Liquide, we recommended a vote against the chair due to the lack of significant progress on the issue, whereas at BP and Rio Tinto we supported the boards in recognition of the progress made, while continuing to engage for improvements. We have also sent letters to other companies where we co-lead the CA100+ engagement, such as Repsol and Mercedes-Benz, emphasising the importance of addressing our expectations and properly recognising the financial materiality of climate risk.

Where does CA100+ go from here?

Although good progress has been made over the last five years of climate engagement, many of the world's biggest emitters are still far from achieving full alignment with the Net Zero Benchmark or the 1.5°C goal of the Paris Agreement. To this end, CA100+ is considering how it might go further in phase two.

EOS has responded to two consultations on strategy renewal for phase two of CA100+ and the development of the Net Zero Benchmark. We support proposals for greater depth of engagement on specific sub-themes and sectoral priorities and increasing the support and involvement of collaborative investors. We also suggested increasing the focus on the regional differences in decarbonisation to support better region-specific engagement.

Given the growing importance of the Net Zero Benchmark, we emphasised the importance of transparent and strong governance processes to support its credibility. We also supported proposals for a rolling assessment process, whereby companies would be assessed at a time that suits their disclosure and AGM timetable.

We will continue to play an active role in CA100+ and other collaborative climate engagements, leveraging the power of collaborative engagement as an escalation tool, and a way to signal investor consensus on the need for rapid climate action from the world's largest emitters. We will continue to shape efforts to expand collaborative engagement on climate change to additional sectors and companies not covered by CA100+.

Q&A: Methane Emissions

Diana Glassman
Sector lead: Oil & Gas

Reducing methane emissions this decade is probably the single most important action the world can take to reduce the rate of global heating. Methane warms the planet about 80 times more effectively than CO_2 over a 20-year period, although after about a decade it starts to dissipate. Making swift reductions in methane would curb rising temperatures more quickly than carbon dioxide cuts in the short term. This buys time for hard-to-abate sectors to find viable technological solutions for their carbon emission problem, helping to limit global warming to 1.5°C.

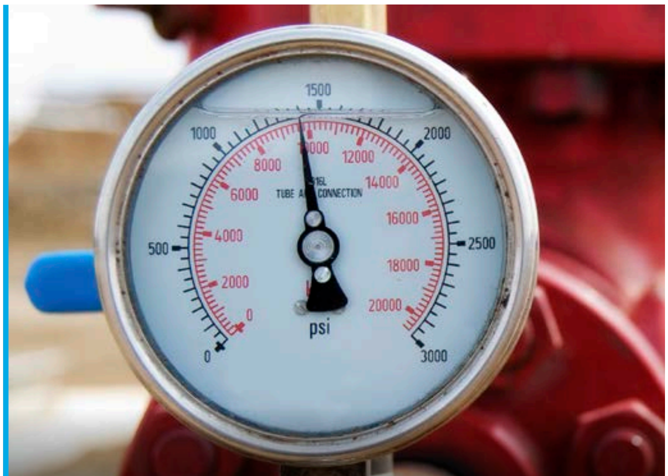
The importance of methane as an effective short-term lever is recognised in key industry scenarios. The International Energy Agency's Net Zero scenario, and its 2022 updated roadmap,[1] assume a 75% fossil fuel methane emissions reduction by 2030. The Oil & Gas Methane Partnership (OGMP) 2.0 calls for a 45% emissions reduction by 2025 relative to 2015 levels, with a 60-75% reduction by 2030.

We have engaged with energy companies on this topic for several years. We intensified this work in 2020 and 2021, to build cross-industry consensus on the actions that need to be taken to help curb methane emissions. We also advocated for the adoption of industry best practice with regulators, and collaborated with trade bodies and environmental advocacy groups to help reduce the wasteful flaring and venting of methane.

Q. How did we address methane reduction in our engagements in 2022?

A. Under the EOS Engagement Plan, we are seeking a 60-75% reduction in oil and gas operational methane emissions by 2030, from a 2015 baseline. To help drive this outcome, we take a system-wide approach to engaging across the value chain with key upstream operators, midstream players who transport oil and gas to market, customers, and financial enablers, as well as speaking to trade associations and regulators. We also focus on increasing transparency across the system so that any progress can be evaluated.

In our engagements with upstream oil and gas companies – the producers – we ask them to make every effort to reduce flaring, venting and fugitive emissions. Leaks can be detected through regular testing and maintenance, for example, while the installation of solar panels can help to replace pneumatic equipment. Encouragingly, 60-80% of the options to curb leaks from the oil and gas sector are low cost, and in many cases, there is an upside. "The greatest potential for negative cost abatement is in the oil and gas subsector where captured methane adds to revenue," the UN Environment Programme (UNEP) states.



In our engagements with upstream oil and gas companies we ask them to make every effort to reduce flaring, venting and fugitive emissions.

Specifically, we ask for methane reduction commitments and implementation plans aligned with the UNEP-managed Oil & Gas Methane Partnership (OGMP) 2.0 to achieve a critical near-term outcome that progresses longer-term decarbonisation objectives. We were an early supporter of the OGMP 2.0, which offers a step-change improvement in the transparency and credibility of reported methane emissions from oil and gas operations. Alignment with the OGMP must be a priority for producers given that it is in their own financial interest.

Q. Can you give some examples of positive outcomes?

A. We have engaged with Occidental Petroleum on methane since 2018 when we asked it to set emissions targets as part of our feedback on the company's first climate change report. In early 2022 we expressed our support for OGMP 2.0 to a director, and the company subsequently formally joined. We also engaged with ConocoPhillips, including in-person at the company's Houston headquarters in early 2022, and we were pleased when it joined OGMP 2.0 later in the year.

We engaged with another US energy company Chevron ahead of its annual shareholder meeting, including in-person with the company's ESG manager and corporate secretary, to urge the board to support a shareholder proposal for a report on the reliability of the company's methane emission disclosures. As Chevron's board eventually decided to support the proposal, in May we filed an exempt solicitation encouraging investors to vote for the board's recommendation.[2] At the meeting, 98% of shareholders voted in support.

[1] World Energy Outlook 2022 (windows.net)
[2] https://www.sec.gov/Archives/edgar/data/93410/000162363222000596/form.htm

Q. What work have we been doing in the public policy sphere?

A. We worked closely with the Environmental Defense Fund (EDF), a US-based non-profit environmental advocacy group, on a letter to send to the International Financial Reporting Standards (IFRS) Foundation. This came in response to the International Sustainability Standards Board's draft IFRS Climate-related Disclosures for oil and gas exploration and production, midstream operators, and electricity and gas utilities and distributors. The letter laid out specific methane-related disclosure enhancements.

Noting that methane emissions are inconsistently and under-reported we submitted a comment letter on the US Environmental Protection Agency's proposed rule on US oil and gas sector methane emissions for new and existing sources, expressing support for strong methane emissions performance standards. We stated our principles-based position in support of enhanced reporting transparency, credibility and comparability and endorsed the OGMP 2.0 disclosure framework.

We also called for the promotion of best operating practices including reducing the wasteful practice of routine flaring, advanced leak detection and the use of zero-emitting pneumatic controllers, along with an improvement of public health and safety and environmental justice.

Q. What progress was made in 2022?

A. Russia's invasion of Ukraine in February 2022 triggered a realignment of global energy supplies. The search for energy security and greater affordability created a unique opportunity to reduce methane emissions in the supply chain.

In a positive development at COP27, the EU, UK, US, Canada, Norway, Japan and Singapore issued a joint declaration from energy importers and exporters on reducing greenhouse gas emissions from fossil fuels.[3] This focuses on reducing methane emissions, and specifically references OGMP 2.0. The joint declaration builds on the COP26 Global Methane Pledge that aims to reduce economy-wide methane emissions by 30% by 2030 from 2020. It also sends a welcome signal that some important Asian customers expect suppliers to dramatically reduce their methane emissions.

Accompanying COP27, many countries announced tighter methane regulations. For example, the US Environmental Protection Agency proposed expanding oil and gas methane regulations to include smaller wells[4] and Canada introduced laws aiming to reduce oil and gas methane emissions by 75% by 2030.[5] Even China, which did not sign the Global Methane Pledge, announced that it would increase monitoring,[6] which is a step in the right direction.

Q. What will we focus on in 2023?

A. As reducing methane emissions has additional social benefits, we will increasingly spell out the links between methane and human rights in our engagement. Methane has deleterious health impacts, contributing to premature deaths, asthma-related hospital visits due to the formation of ozone at ground-level, and lost labour due to extreme heat. Curbing methane emissions to mitigate climate change, which disproportionately impacts those least able to adjust to it, would help to avoid exacerbating existing inequities that create an additional layer of long-term risk for investors.

At the same time, we will continue pushing upstream and midstream companies to take responsibility for emissions in their joint ventures in addition to their operated assets, and to sell assets only to parties who will adhere to best practices in methane emissions management and reporting.

Engagement with demand-side consumers of methane and banks will be amplified. Big users of oil and gas, such as utilities, cement manufacturers and petrochemical companies, should also be demanding transparency from upstream suppliers on this issue, given the slow pace of mitigation to date and the limited timescale in which to act. Financial institutions should focus on urging public and private clients to include rapid methane emissions reduction in their energy transition plans and urge them to join OGMP 2.0.

We will continue to engage with companies and policymakers to encourage a switch to renewable energy, and an overall reduction in demand for fossil fuels. In parallel, we will push fossil fuel companies and trade associations to develop collaborative solutions that reduce actual methane emissions and have a real near-term impact on climate outcomes.

[3] Joint declaration from energy importers and exporters on reducing greenhouse gas emissions from fossil fuels - GOV.UK (www.gov.uk)
[4] Biden-Harris Administration Strengthens Proposal to Cut Methane Pollution to Protect Communities, Combat Climate Change, and Bolster American Innovation | US EPA
[5] Canada, Nigeria target oil and gas methane emissions with new laws | Reuters
[6] China announces plan to curb rising methane emissions but challenges await | Reuters

Can banks become net-zero heroes?

With some of the world's biggest banks still financing fossil fuel expansion, we collaborated on a key initiative to help investors assess banks on their low-carbon transition strategies and hold them to account.

Banks have come under fire for pouring US$4.6tn into fossil fuels since the Paris Agreement was signed,[1] sometimes while vigorously promoting their green credentials. HSBC was censured by the UK's advertising watchdog in October 2022 for a misleading campaign that highlighted how the bank had invested $1tn in climate-friendly initiatives, while failing to acknowledge its own contribution to emissions.[2]

It's a problem that investors and their representatives also have to wrestle with when assessing how much a bank is really doing to help support the transition to a low-carbon economy. Banks are significant allocators of capital and serve as financiers for the most carbon-intensive sectors and operators. But they can also play a critical role in supporting their corporate clients in transitioning their operations. Some banks have signed up to the industry-led, UN-convened Net-Zero Banking Alliance (NZBA), which aims to accelerate the implementation of decarbonisation strategies.[3]

While this has been well-received, it creates new challenges for investors. Assessing a bank's commitments and transition strategy performance versus those of its peers, and the alignment of bank strategies with science-based pathways to limit climate change to a 1.5°C warming scenario, is challenging. Many large financial institutions have committed to achieving a similar net-zero emissions by 2050 vision, including portfolio-related Scope 3 financed emissions from banking activity. But there is some variation in the approaches taken to setting 2030 interim reduction targets for financing. Also, there is little clarity regarding immediate-term implementation, or how these considerations inform transaction-level decision-making.

Building a framework

To help investors assess banks on their transition strategies and align their own portfolios with net zero, the Institutional Investors Group on Climate Change (IIGCC) and the Transition Pathway Initiative produced the Net Zero Assessment Framework in July 2022.[4] EOS at Federated Hermes, continuing our role as a co-chair for the IIGCC Banks Working Group, contributed directly to the finalisation of this framework. This followed our work on the banking sector investor expectations published in April 2021.[5] That document set expectations for banks to manage climate-related risks and opportunities by aligning their activities with the goals of the Paris Agreement.

Our contribution to the Net Zero Assessment Framework included giving direct and specific feedback on the scoring methodology, co-authoring the report foreword, and contributing to the socialisation of the framework. It includes pilot indicators under six key areas underpinning a bank's approach to the transition. These are long-term commitments, short- and medium-term targets, decarbonisation strategies, climate governance, policy engagement, and audit and accounts.

The framework was designed to enable investors and their representatives to robustly engage on bank transition strategies, as part of their own net-zero alignment efforts and stewardship of portfolio companies. Through the

Emily DeMasi
Sector lead: Financial Services

[1] https://www.ran.org/wp-content/uploads/2022/03/BOCC_2022_vSPREAD-1.pdf
[2] https://www.theguardian.com/business/2022/oct/19/watchdog-bans-hsbc-ads-green-cop26-climate-crisis
[3] https://www.unepfi.org/net-zero-banking/
[4] https://www.iigcc.org/media/2022/07/An-investor-led-framework-of-pilot-indicators-to-assess-banks-on-the-transition-to-net-zero-28-July.pdf
[5] https://www.iigcc.org/download/investor-expectations-for-the-banking-sector/?wpdmdl=4454&refresh=62d672fa4e52e1658221306

development of this framework, we support the shift in investor engagement to go beyond a focus on a high-level commitment, towards practical tactics and implementation.

Using the framework in engagement

The results of the initial benchmarking exercise against the six pilot indicators showed a significant gap between global financial sector best practice and what is needed to align with 1.5°C. We found these results helpful in highlighting opportunities for improvement, which we could then cite when engaging with the evaluated banks. The framework has also been useful when engaging with banks that are lagging behind and still considering how to build a comprehensive climate strategy.

We have referenced the Net Zero Assessment Framework in direct and collaborative engagements, particularly in discussions around a bank's transition strategy. For example, we engaged with First Citizens Bank to discuss updates to its ESG strategy following its merger with CIT Group. Following the merger, the bank has significant commercial relationships in addition to an extensive retail banking portfolio, and is determining how its ESG strategy should look. We pointed to the Net Zero Assessment Framework when articulating the expectations we have for portfolio-related climate strategy and encouraged the bank to build its decarbonisation strategy and climate governance, in addition to considering emissions reduction targets.

As part of our work to support the framework, we helped to ensure that all the collaborating investors and evaluated banks were made aware of the analysis and methodology, facilitating a bank-wide webinar series to communicate the results and a way forward for the assessment. We also directly contributed to the feedback process informing the next iteration of the framework, to be released in Q2 2023.

To help bring the framework to a wider audience, we have taken part in public events. During New York Climate Week, we participated in the Intentional Endowments Network Roundtable at the Nest Summit, featuring in the Climate Justice and Net Zero panel discussion. When asked about the role of banks within the low-carbon and just transitions, we referenced the Net Zero Assessment Framework as a helpful tool that articulates some of the important components of a bank's strategy. And during the Ceres Financing a Net Zero Economy event in Manhattan, we again referenced the Net Zero Assessment Framework when explaining how investors could engage with banks regarding their transition strategies.

It is important for companies to develop strategies to reduce their emissions footprint, but they should also recognise where they are reliant on significant public policy and technology development.

Outlook for 2023

In 2023, we aim to drive the second iteration of the framework and contribute to elements reflecting the just transition. We will continue our co-chair role with the IIGCC to contribute to how the collaborative drives engagement on implementation and tactics that enable progress against net-zero commitments. As the framework evolves and banks begin to respond to the areas outlined across the pillars, there is the potential for us to leverage this resource to inform our vote policy.

During New York Climate Week, we participated in the Intentional Endowments Network Roundtable at the Nest Summit, featuring in the Climate Justice and Net Zero panel discussion.

Q&A: Just Transition

Emily DeMasi
Theme co-lead: Human Capital

The concept of a "just transition" has been around since the 1980s, but it was elevated at the COP26 climate summit in 2021 as a critical factor to support the phase out of fossil fuels and the ramp up of clean energy.[1] A just transition means moving towards a low carbon economy while keeping workers, communities and those most adversely impacted by the climate transition at the heart of decision-making.

It includes reskilling and relocating workers where possible, consulting with and incorporating community needs for project development and closures, and seeking and obtaining free and informed prior consent from indigenous peoples, who are often impacted by energy projects on their land. It goes beyond mere consideration of climate impacts to include health and equity impacts, and provides opportunities for an inclusive and equitable climate transition through appropriate mitigation of the social risks associated with transition plans.

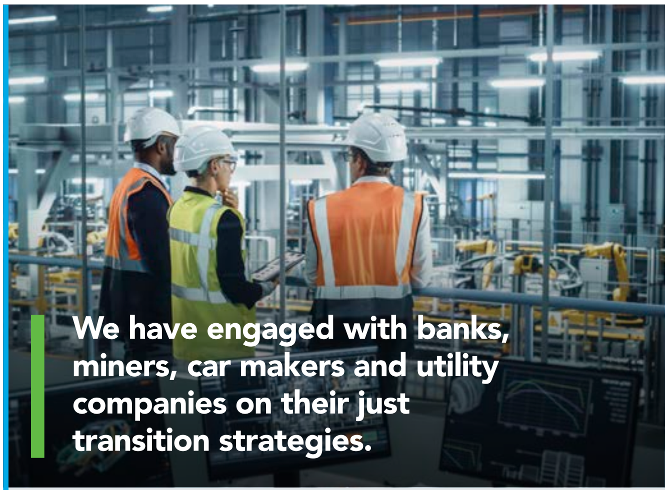
Q. Why is it important?

A. Transitioning to a low carbon economy will have a profound impact on workers, their families and certain communities, especially in the energy and transportation sectors. Without consideration of a just transition, we risk marginalising communities and demographics already disproportionately impacted by climate change, such as women and people of colour. At the same time, opportunities to lay the social groundwork for a resilient net-zero economy may be missed.

Working with impacted stakeholders helps companies, regions and countries to understand the positive and negative impacts of bold climate action, and identify the best solutions for their context. These should support a green jobs revolution in which the newly-created jobs have guaranteed living wages, proper workplace safety protections, and health benefits.

Q. How have we engaged with companies on this issue? What did we ask for?

A. We have engaged with banks, miners, car makers and utility companies on their just transition strategies. We believe that companies should disclose clear just transition plans with timelines to complete the transition. They should conduct impact assessments on the workforce, communities and other stakeholders most



impacted by their carbon transition, resource the transition plan with a taskforce and proper oversight, and collaborate with governments and NGOs to facilitate a just transition.

Q. Can you give some examples of positive outcomes?

A. We see some companies articulating a just transition. For example, we engaged with the US utility American Electric Power (AEP), asking for the disclosure of a clear just transition plan as it retires some assets, an assessment of the impact on the workforce, and a timeline to complete the transition. We were impressed by the company's detailed just transition section within its 2021 Climate Impact Analysis report.

The company has formed a special transition taskforce and partnered with a local NGO, the Just Transition Fund, to facilitate a dialogue for the retirement of the coal-fired Pirkey Power Plant. It has helped 75% of the workers in the plant to move to other positions, either with or outside the company, or to retire with the plant. We will continue to engage with the company on its just transition plans for retiring additional coal plants and on its assessment of potential unintended social consequences in the supply chain.

[1] What is just transition? And why is it important? | Climate Promise (undp.org)

Q. Why were Canadian banks in the spotlight in 2022?

A. We consider just transition plans that include specific strategies for communities more heavily exposed to the fossil fuel industry and people disproportionately impacted by climate change to be a core tenet of human rights. Canada faces a unique challenge as it transitions to a low carbon economy as it is heavily exposed to the energy sector, and has exhibited faster warming and greater climate change vulnerabilities than the rest of the world.[2]

Meanwhile, Canadian banks continue to finance fossil fuels, and their own net-zero climate commitments are contingent upon their ability to help clients and communities achieve their own transition plans.

> **Canada faces a unique challenge as it transitions to a low carbon economy as it is heavily exposed to the energy sector, and has exhibited faster warming and greater climate change vulnerabilities than the rest of the world.**

Q. How did we engage with this sector?

A. To advance this engagement, we made coordinated statements during the 2022 annual shareholder meeting season at Royal Bank of Canada, Toronto-Dominion, Bank of Nova Scotia, Bank of Montreal and Canadian Imperial Bank of Commerce, addressing the banks' climate strategies as they relate to a just transition. Our aim was to broaden the conversation from a pure focus on environmental net-zero 2050 targets to encompass larger human rights impacts. We also highlighted the guidance from our work with the Institutional Investors Group on Climate Change (IIGCC) in developing investor expectations for the banking sector.

We asked the banks to make an explicit commitment to achieving a just transition, paying attention to the impacts and opportunities for key stakeholders, including workers, their families and the communities most impacted by the low carbon transition. We also asked for reporting on the specific actions the banks would take to achieve the just transition, being clear on how borrowers' own commitments, capacity and strategy to achieve the just transition were factored into financial decision-making.

Q. What have we advocated for with policymakers and regulators?

A. In our 2022 comment letter to the US Securities and Exchange Commission (SEC) regarding the enhancement and standardisation of climate-related disclosures for investors, we recommended that the SEC require disclosure on climate change impacts to communities and workers, and the just transition.[3] We cited the rights of indigenous peoples as particularly relevant to climate change as they often reside in areas that are central to energy production and transmission. We highlighted the potential risk for investors that arises from the failure to obtain free, prior, and informed consent (FPIC) as one reason to include just transition plans as part of enhanced standardised climate-related disclosures.

Q. What will we focus on in 2023?

A. We will continue to engage banks on their just transition plans with a focus on FPIC and the specific actions banks can take to achieve the just transition, including how these are factored into financial decision-making. We will also pursue other sector-specific engagement as it relates to the just transition including employee training and upskilling in those industries most at risk for disruption, such as car manufacturing, as plants switch to electric vehicles. Other considerations include community support as coal mines close, and green energy affordability to tackle global energy poverty.

[2] Canada warming twice as fast as the rest of the world, report says - BBC News
[3] s71022-20131951-302407.pdf (sec.gov)

CASE STUDY

LyondellBasell

We have engaged with multinational chemical company LyondellBasell on climate change since 2017. As part of Climate Action 100+, a collaborative engagement of more than 370 investors and their representatives seeking greenhouse gas emissions reductions from the world's largest emitters, we co-lead the engagement with the company.

LyondellBasell first published its sustainability disclosures and CDP reports in 2017. These disclosures were useful but did not set targets. In 2019, our feedback on the company's sustainability and CDP reports highlighted the lack of forward-looking targets for energy efficiency, carbon emissions, effluents, water efficiency and waste, and meaningful solutions for sustainable plastic use.

In Q2 2020, in a meeting with senior executives, the company acknowledged our request for forward-looking targets, including science-based targets, and said it was investing in energy efficiency projects. Together with CA100+ investors and their representatives, we met the CEO and senior management in Q2 2021 to discuss the company's progress towards disclosing sustainability targets, including its planned science-based targets and a net-zero ambition.

In order to accelerate progress, as the CA100+ lead for the company, we used a legal mechanism to propose a discussion on climate change at the company's 2021 annual meeting. EOS led contributions by a group of eight institutional investors who questioned climate progress leading to over 45 minutes of shareholder-board discussion on the company's climate change strategy. During the meeting the company indicated its willingness to make further commitments.

Changes at the company

In Q3 2021, we welcomed the company's release of its climate strategy, setting a Scopes 1 and 2 net-zero ambition for its global operations by 2050; a 30% absolute reduction of Scopes 1 and 2 emissions by 2030; and a goal to source a minimum of 50% of its electricity from renewable energy by 2030.

In addition to its climate goals, LyondellBasell prioritised actions in its 2020 sustainability report to help eliminate plastic waste from the environment including waterways and oceans and to advance a circular economy.

The company has a goal to produce and market two million metric tons of recycled and renewable-based polymers annually by 2030. To deliver on this ambition, it recently announced a new organisational structure including a Circular and Low-Carbon Solutions business segment, and is strategically investing along the value chain. While a quantifiable water goal was not set by the company, water management efforts are well covered in the sustainability report.

It has also set out a pathway towards achieving its 2030 target and we encouraged LyondellBasell to collaborate with industry peers with the aim of developing a science-based sector-wide Scope 3 approach. In late 2022, LyondellBasell announced that it would increase its 2030 greenhouse gas emissions reduction target for Scopes 1 and 2 emissions to 42%, relative to a 2020 baseline. It also said it would establish a 2030 Scope 3 greenhouse gas emissions reduction target of 30%, relative to a 2020 baseline, and in accordance with guidelines from the Science Based Targets initiative (SBTi). It will submit its climate goals to the SBTi to be validated against SBTi guidance.

Next steps

We continue to engage with LyondellBasell on its pathway to net zero including capital allocation and climate policy. We note the company's pathway to net zero will require shorter-term adjustments, such as energy/material efficiency improvements or switching to renewable energy, as well as longer-term solutions including hydrogen. We expect to see greater clarification and detail from the company on how climate transition pathways contribute to its net zero ambitions and align with capital expenditure plans, financial accounting and audit, and just transition.

Joanne Beatty
Sector lead: Chemicals

Q&A: Deforestation, Biodiversity and Sustainable Food Systems

Sonya Likhtman
Theme co-lead: Climate Change

Zoe de Spoelberch
Theme lead: Natural Resource Stewardship

With COP 15 finally going ahead in Montreal in December 2022 after multiple postponements, the threat to wildlife and natural habitats remained in focus for investors last year. Biodiversity supports the ecosystem services on which we all depend - clean air, productive soils, clean water, food supplies and carbon dioxide absorption to mitigate global warming. Biodiversity loss therefore presents a grave threat to the survival of humanity and economic activity.

Five out of nine planetary boundaries, which define a safe operating space for human existence, have been crossed already. These include biodiversity loss and other contributors such as climate change and land conversion. This highlights the urgency of protecting and restoring biodiversity.

We have responded to this challenge by engaging with companies on their impacts and dependencies on biodiversity, and encouraging them to develop strategies to avoid and mitigate their impacts on nature, whilst aiming for an overall net-positive impact. We have also developed a dedicated biodiversity engagement programme for companies in the food and beverage sector to encourage better stewardship of nature. Through the year we continued to advocate for best practice and industry standards, including calling for an ambitious Global Biodiversity Framework at COP 15.

Q. In which sectors is biodiversity an important factor to consider, and why?

A. The food system is the primary driver of biodiversity loss due to its high impacts and dependencies on the natural world and ecosystem services. Food producers are reliant on healthy soils, natural pollination and the availability of clean water to grow their crops, with 75% of the world's crops requiring natural pollination.[1] Food producers and manufacturers also have high impacts on biodiversity through their operations and supply chains, with some 75% of agricultural land used for animal grazing or growing crops for animal feed.[2] Over 15% of global greenhouse gas emissions come from animal agriculture, equivalent to those from all transportation combined, while total food production accounts for around 37% of emissions.[3,4]

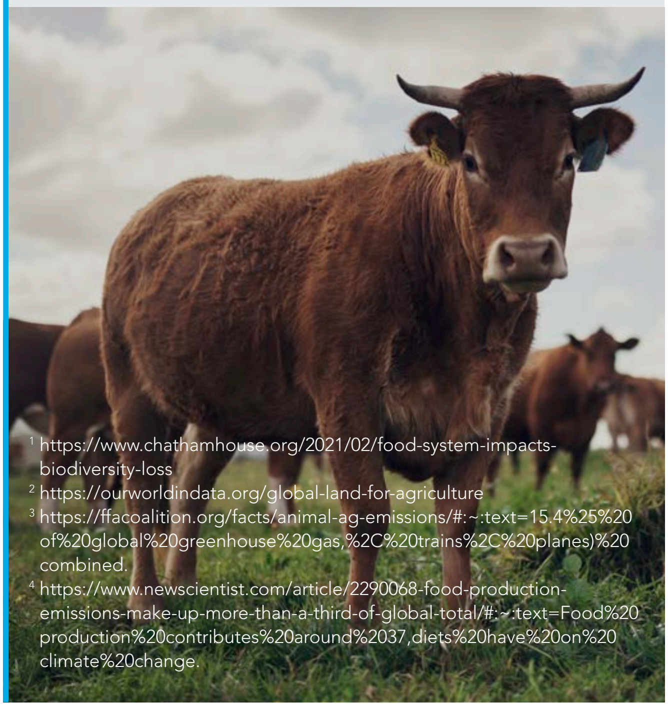
Q. How did we address this through engagement?

A. We developed a dedicated biodiversity engagement programme to accelerate and deepen the focus on biodiversity protection and restoration. The programme includes 15 companies from the food and beverage sector from around the globe. The selection process for the target companies was based on multiple factors, including laggard companies on the Forest 500 or Farm Animal Investment Risk and Return (FAIRR) benchmarks, companies with low ratings on the World Benchmark Alliance Seafood Index, or those selected as having poor water-related performance as part of the Ceres Valuing Water Finance Initiative. We also looked at companies with controversies related to biodiversity, such as inappropriate antibiotic use and animal welfare concerns.

To begin the engagement, we sent a letter to each company outlining the risks of not addressing biodiversity loss. We also held individual and collaborative engagement meetings to highlight our expectations and discuss how each company could contribute to halting and reversing nature loss.

Other sectors for which biodiversity loss is material include infrastructure, banking and financial services, fast fashion, chemicals and extractives, due to their operational and supply chain impacts on biodiversity. In our engagements, we are integrating more biodiversity discussions for these sectors to progress cross-industry action on biodiversity.

Material issues for engagement include regenerative agriculture, deforestation, sustainable proteins, water use, animal welfare, antimicrobial resistance, chemicals and pollution, and ocean health. The key topic for us is deforestation, as it has the most related metrics and certification schemes across the industry.



[1] https://www.chathamhouse.org/2021/02/food-system-impacts-biodiversity-loss
[2] https://ourworldindata.org/global-land-for-agriculture
[3] https://ffacoalition.org/facts/animal-ag-emissions/#:~:text=15.4%25%20of%20global%20greenhouse%20gas,%2C%20trains%2C%20planes)%20combined.
[4] https://www.newscientist.com/article/2290068-food-production-emissions-make-up-more-than-a-third-of-global-total/#:~:text=Food%20production%20contributes%20around%2037,diets%20have%20on%20climate%20change.

Q. Why should companies integrate biodiversity into their strategies and what are our expectations for them?

A. Companies with impacts and dependencies on biodiversity are exposed to numerous risks. These include operational risks, which occur when companies face direct challenges in sourcing raw materials due to disruptions to ecosystem services. For example, farmers may be unable to supply raw ingredients due to a lack of water availability or unhealthy soils.

Companies may also face reputational risks and lose their social licence to operate if they are found to be responsible for having negative impacts on biodiversity. This has occurred to companies linked to deforestation in the Amazon, for example. Another type of risk is transition risk, which occurs when companies fail to capitalise on opportunities by not effectively taking nature into account in their decision-making. For instance, food and beverage companies may not respond to the growing consumer demand for healthy, plant-based or organic foods.

Another risk on the horizon is the regulatory and litigation risk that companies may face relating to biodiversity. The UK and EU deforestation due diligence laws require companies to ensure that commodities have been sourced without links to illegal deforestation. We have also seen articles in French law requiring large companies and financial institutions to disclose their biodiversity risks and impacts. We expect regulation around biodiversity to increase over time.

Our white paper on biodiversity, *Our Commitment to Nature,*[5] published in early 2021, outlined our expectations on biodiversity. Priority actions include identifying, assessing and disclosing a company's impacts and dependencies on biodiversity, and committing to having a net-positive impact or no negative impact on biodiversity throughout a company's operations and supply chain by 2030. Companies should also establish a strategy to address their most material biodiversity impacts and dependencies, and articulate a plan with milestones to deliver this.

Food producers are reliant on healthy soils, natural pollination and the availability of clean water to grow their crops.

Following our engagement, Posco International began a discussion with the Roundtable on Sustainable Palm Oil.

Q. One of the material issues we engage upon is deforestation. How do we address this?

A. Deforestation has a material impact on climate change and biodiversity loss. Federated Hermes Limited signed a commitment at COP26 to seek best efforts to eliminate deforestation by 2025 through engagement and due diligence. Through the Finance Sector Deforestation Action (FSDA)[6] collaborative initiative that followed this commitment, we sent letters to multiple companies outlining deforestation risks and asking for engagements. We will continue engaging with relevant companies including palm oil producers, processors, traders, consumer goods and retail companies, and banks providing financing.

Q. Can you give some examples of company engagements?

A. We encouraged companies including Meiji Holdings, Yakult Honsha, Asahi Group, Saputo, Kellogg's and General Mills to commit to zero deforestation by 2025 for all commodities, regions and suppliers, including indirect suppliers. We discussed how this commitment would be implemented through certification, traceability and due diligence.

Following our engagement, Posco International began a discussion with the Roundtable on Sustainable Palm Oil (RSPO) to develop its sustainable palm oil strategy. In 2022, it confirmed that its palm oil subsidiary's no deforestation, no peat, no exploitation (NDPE) policy was being implemented in close cooperation with the RSPO and that it had developed a large-scale environmental conservation and community development programme in accordance with RSPO guidelines.

[5] https://www.hermes-investment.com/be/fr/professional/eos-insight/stewardship/our-commitment-to-nature/
[6] https://climatechampions.unfccc.int/system/nature-and-tackling-deforestation/

We have also escalated our engagement on deforestation to annual shareholder meetings. We hold the chair or other responsible directors accountable through voting recommendations where we believe companies' actions are materially misaligned with limiting global warming to safe levels, including through links to deforestation. In 2022, we recommended votes against directors at TJX, Kikkoman Corp and WH Group. We also included financial institutions in our policy for the first time, which led to recommendations to vote against directors at Power Corporation of Canada, Malaysia's Public Bank and Industrial and Commercial Bank of China due to concerns about deforestation.

Q. Can you highlight any positive outcomes?

A. We can see that biodiversity is becoming a bigger priority for some companies, although there is still a lot of work to be done. Some companies are starting to identify their impacts and dependencies on biodiversity and we have encouraged companies to prepare for the Taskforce on Nature-related Financial Disclosures (TNFD). For example, in an engagement with Meiji Holdings, we were pleased to hear the company express an upcoming focus on measuring its impact, especially in anticipation of future developments of the TNFD.

We have also engaged extensively on regenerative agriculture.[7] We expect companies to increase the use of these methods in their direct and indirect supply chains to source a significant proportion of total ingredients through these sustainable techniques. Best practice is for companies to document the benefits and outcomes of their regenerative agriculture strategy on biodiversity, soil health, carbon sequestration, crop yields, water flow and other focus areas, with relevant KPIs tracked and disclosed.

We were impressed by Carrefour's regenerative agriculture pilot and urged the company to scale its work to a larger proportion of its supplier base. Similarly, General Mills set a goal of advancing regenerative agriculture on one million acres of farmland by 2030 and we encouraged the company to scale its ambition across its suppliers and the industry. We also discussed regenerative agriculture with Kellogg's and challenged it to strengthen its commitment by setting a target on the amount of land or proportion of ingredients sourced using regenerative agriculture techniques. With Saputo, we discussed the importance of increasing the focus on sustainability within the supply chain. We encouraged the company to set expectations and support suppliers on carbon, deforestation, pesticide use and other aspects of sustainable agriculture.

We also engaged with the chief sustainability officer of Yum! Brands to encourage the company to set a group-level target and develop a strategy for sustainable proteins. We understand that the demand for sustainable protein is growing in Europe, but that animal-based products remain very popular in North America. We asked the company to perform pilots and use marketing strategies to encourage consumers to choose more plant-based foods. We also engaged with the head of sustainability at Salmar, asking the company to replace marine ingredients with plant-based ingredients in its salmon feed, to protect ocean health.

Q. What did we advocate for ahead of COP 15?

A. As co-chair of the Finance for Biodiversity Foundation's public policy and advocacy working group, we advocated for an ambitious Global Biodiversity Framework (GBF) to be agreed at COP 15. We focused on the need for the GBF to require public and private financial flows to be aligned with global biodiversity goals and targets. We also contributed to three position papers outlining text suggestions for the GBF. We attended international biodiversity negotiations virtually in August 2021, in Geneva in March 2022, and in Montreal in December 2022.

Sonya Likhtman at COP 15 in Montreal.

At COP 15 the Kunming-Montreal Global Biodiversity Framework was adopted by almost 200 countries. This features a target to protect at least 30% of land and seas by 2030, and addresses key issues related to biodiversity loss, such as subsidies and the financing gap. There is a requirement for financial flows to be aligned with both the 2030 targets and the 2050 vision, which should stimulate action over the short, medium and long term. In addition, governments will be required to ensure that large companies and financial institutions assess and disclose their risks, impacts and dependencies on biodiversity throughout operations, value chains and portfolios.

Q. What can we expect for 2023?

A. The focus is expected to turn to implementing the GBF at the national level in areas such as deforestation, sustainable agriculture, and disclosure of impacts and dependencies. With the TNFD framework expected to be finalised in Q3 2023, more companies should start to disclose information about their nature-related risks and opportunities in a standardised and decision-useful manner.

Companies and investors should continue to improve their understanding of the importance of addressing biodiversity loss alongside climate change. Collaboration across the industry will be essential for solving ongoing challenges and tackling the biodiversity crisis with the urgency it requires. We will continue to prioritise this topic through engagement, advocacy and active participation in industry initiatives.

[7] https://www.hermes-investment.com/uk/en/institutions/eos-insight/stewardship/how-regenerative-agriculture-can-sow-the-seeds-of-change/

Social & ethical

Engaging on the rising cost of living

Soaring food and fuel price inflation squeezed household budgets in 2022, driven by supply chain disruption, Russia's invasion of Ukraine, and labour shortages in key sectors such as logistics. Justin Bazalgette explains how we engaged with companies to help mitigate the worst impacts.

Justin Bazalgette
Theme co-lead: Corporate Reporting

Life became a lot more expensive in 2022. As economies emerged from the pandemic and companies tried to ramp up production, components shortages and a lack of delivery drivers presented a severe headwind.[1] The unprecedented disruption in supply chains caused by the Covid-19 pandemic created global shortages for key parts, while the logistics sector and airports struggled to recruit workers, having made redundancies during the pandemic. People taking early retirement, the impact of long covid, and in the UK, the departure of EU workers, also led to the disappearance of significant numbers from the workplace, with healthcare and hospitality among the hardest hit sectors.[2]

Russia's invasion of Ukraine in February 2022 triggered a surge in energy prices, and impacted food ingredients such as sunflower oil and wheat. Frequent price hikes by supermarkets for staples such as margarine, bread and milk have hit the lower-waged hardest.[3] Central banks have responded to inflation by raising interest rates, impacting borrowing costs, with many countries now forecasting low growth or recession. This has created a cost of living crisis, with household budgets under severe strain, prompting workers in some sectors to seek a pay rise to match inflation.

Stretching the household budget

The crisis is having a disproportionate impact on low-waged households as they spend a larger proportion of their income on basic necessities, such as fuel and food. According to the Living Wage Foundation, there are an estimated 4.8 million workers in the UK earning a wage that is below the cost of living. Some 42% of these report missing meals regularly due to financial reasons and 56% say they frequently use foodbanks.[4] During the winter months, people may face the bleak choice of whether to heat or eat.

Financial worries can have a long-term impact on an individual's mental and physical health,[5] and workers under financial pressure are unlikely to perform at their best. This means that businesses could face reduced productivity, higher turnover and increased training costs at a time when they can least afford it. In unionised sectors and companies, a breakdown in relations between management and the workforce may lead to strike action. This can have a negative impact on other businesses that are disrupted, particularly if the dispute becomes prolonged.

Governments have a responsibility to ensure that their citizens' basic needs are met, and that their human rights are protected. While some governments have responded to the energy crisis with price caps[6,7] and energy reduction measures,[8] energy bills are more than double what they were a year ago. Combined with the rising cost of food, motor fuel, housing costs, and other basic expenses, this has meant extreme hardship for certain segments of the population in many countries.

[1] How the COVID-19 pandemic has changed supply chain practices | World Economic Forum (weforum.org)
[2] 7 Industries Experiencing Labour Shortages in 2022 - CXC Global
[3] Inflation for poorest households likely to increase even faster than for the richest, and could hit 14% in October | Institute for Fiscal Studies (ifs.org.uk)
[4] 'Life on Low Pay' https://www.livingwage.org.uk/sites/default/files/Life on Low Pay 2022.pdf
[5] UK private sector between £53-56bn in 2020-21
[6] What is the energy price cap? - MoneySuperMarket
[7] EU proposes to cap 'excessive and volatile' gas prices this winter | Energy industry | The Guardian
[8] Action and measures on energy prices (europa.eu)

Our engagement approach

In recognition of these pressures, we integrated cost of living engagements into our wider stewardship programme in 2022. We challenged companies on their role during this difficult time, encouraging them to assess the impacts of their business models on their stakeholders, and to articulate the actions they could take to help support the most affected, without damaging their long-term sustainability.

Companies need to balance the various pressures in their value chain and steer a responsible course through crises. We encourage companies to consider paying the real living wage,[9] as demonstrated by our voting recommendations, to be creative in meeting the challenges[10] at different levels in their organisation, and to think carefully about how they can support their employees with other benefits. This includes exercising restraint over executive remuneration, similar to the approach taken during the height of the pandemic.[11]

With UK supermarket chain Sainsbury's, we supported the company's adoption of the Living Wage for 90% of its workforce (see box). It also brought forward its 2022 annual pay review to help offset rising cost pressures for employees. We challenged Marks & Spencer on its decision not to subscribe to the Living Wage Foundation, but were reassured that it was working on different cost of living proposals that could achieve an equivalent wage package, such as increased shopping discounts for employees and families. The Royal Bank of Canada confirmed that it would increase its total rewards package to support employees, including a mid-year 3% base salary increase, enhanced family benefits and the offer of mental health/wellbeing support.

Companies also need to work with their suppliers to ensure that rising cost pressures are managed effectively, so that they can continue to provide quality goods while maintaining health and safety standards and conditions of employment.[12] It may not be viable for the full increase in operational costs and wholesale prices to be passed on to customers, as low income households will struggle to absorb this inflation.[13]

Our engagement with FTSE 100 company Ashtead, which operates an equipment rental company in the UK, US and Canada, showed that businesses that treat their employees well during a crisis are able to reap the dividends. By bringing forward pay reviews and paying the living wage, it has maintained staff engagement. Meanwhile, its customers are shifting from purchasing heavy plant to rental models, which has benefitted Ashtead.

Through our discussions with catering group Compass, we learned that there were opportunities to help customers reduce costs by shrinking the number of menu options, flexing opening hours and reducing food stations. At the same time, higher costs from suppliers and higher wages – Compass is a living wage employer – could be covered. Pharmaceutical company Novartis had already made some changes for its workforce in conjunction with its works council, but we encouraged it to consider executive pay restraint in the coming year to ensure a perception of fairness in the eyes of stakeholders.

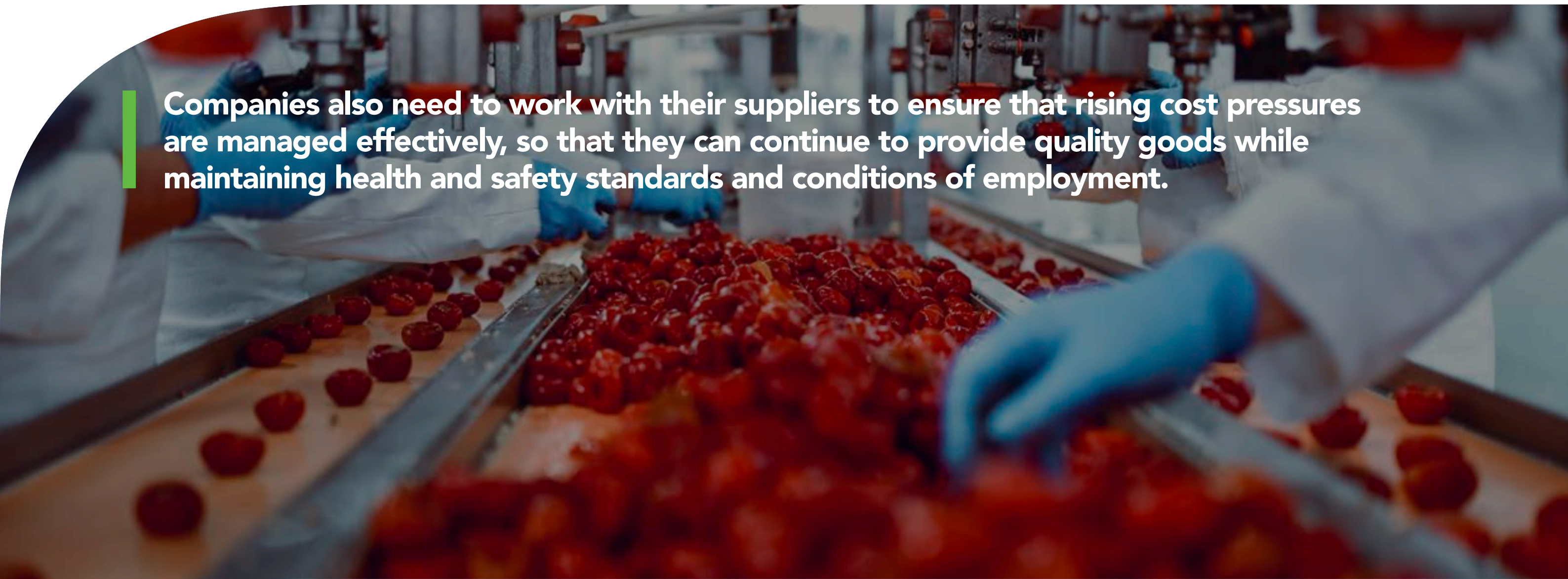
Support for customers

Some sectors have a greater opportunity to cushion the blow for struggling households and small businesses, perhaps by providing some breathing room in a payment schedule. For example, banks can consider the impact of higher interest rates for borrowers, and a potential rise in defaults, while energy utilities can provide more affordable social tariffs for the most vulnerable.

The Commonwealth Bank of Australia has introduced a tiered level of support for customers, with the flexing of contract conditions, and a review of options to help minimise or manage the impact of rate rises. On the utilities side, Centrica is creating a fund to help customers who are struggling to pay their energy bill and Duke Energy is increasing the availability of funds to support struggling customers, as well as highlighting flexible payment options.

Grocery stores can also expand the availability of their own-brand ranges – which usually sell at a significant discount to branded products – to help customers make their money go further. In our engagement with retailers we found that customers were already migrating to lower cost, own-label brands.

How companies balance the trade-offs between rising operational costs and the costs to consumers with the need to generate profits and make pay-outs to shareholders[14] will impact the length and depth of the crisis. A responsible and well-communicated approach will be highly valued by investors from a governance and risk perspective, and may help to strengthen a company's brand value over the long term.



The Living Wage

At a time when real wages are shrinking due to high inflation, how a company responds will be critical for maintaining a healthy, engaged and motivated workforce. Signing up to the real living wage is one way that companies can support employees through a difficult period.

What is a living wage?

- A living wage can be defined as a socially-acceptable level of income that provides adequate coverage for basic necessities such as food, shelter, child services, and healthcare, plus a small margin for unforeseen events.[15]
- The living wage should not be confused with the minimum wage, which is the lowest amount of money that someone can earn as mandated by law.
- Supporters of living wages say they boost productivity and employee morale while critics argue that they could hurt the economy and force companies to reduce their hiring.

Typically we will engage with companies on employee remuneration and encourage accreditation by the Living Wage Foundation in the UK, or similar organisations such as the Global Living Wage Coalition. However, we also recognise the need for wage restraint to control inflation. This means focusing pay increases at the lowest levels, while demonstrating pay constraint at higher levels. This provides a more nuanced approach to remuneration that supports those hardest hit by inflation.

A shareholder resolution was filed at Sainsbury's 2022 annual shareholder meeting calling for the grocery chain to seek accreditation from the UK Living Wage Foundation. In line with our ongoing engagement with the company on the payment of living wages for its workforce and third-party contractors, we gave the resolution careful consideration and engaged intensively with the company – including with the chair, CEO and HR director – to understand its concerns about seeking accreditation.

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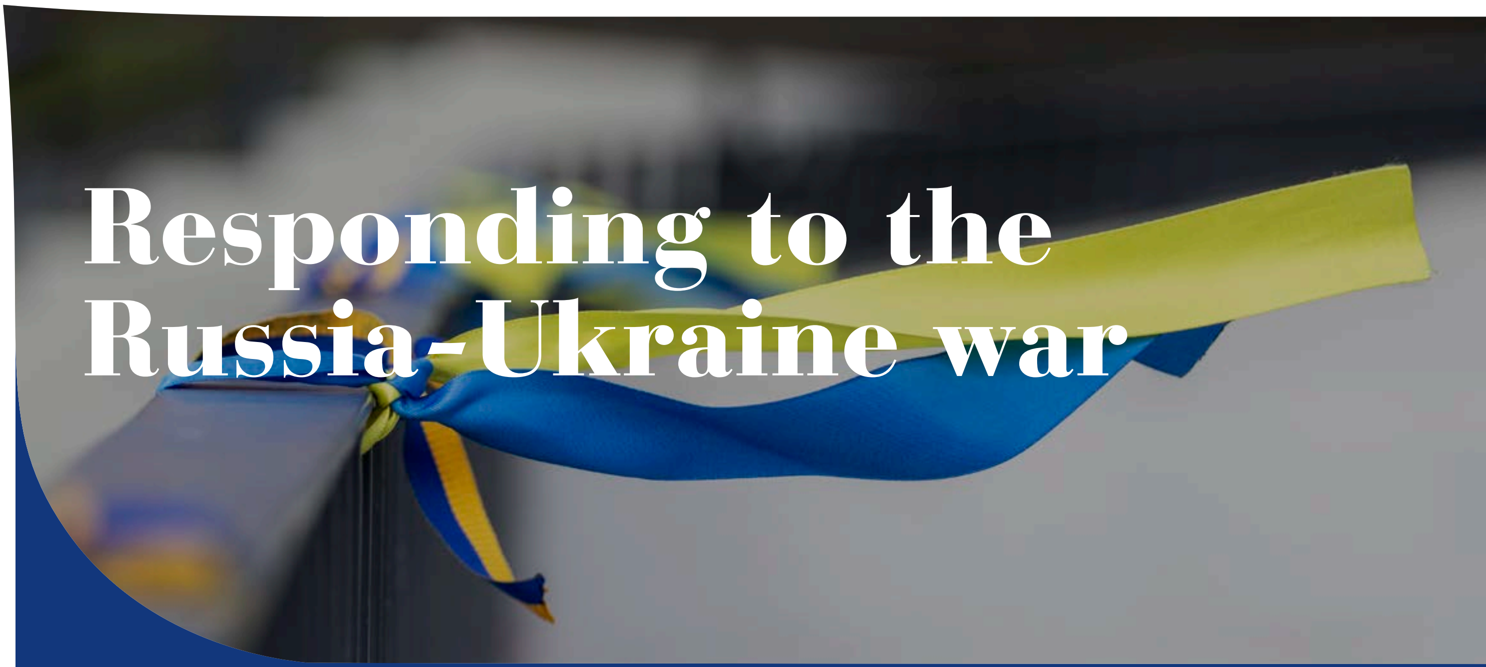
We understood that Sainsbury's already paid the vast majority of its workforce at or above that level, and believed that the majority of its contractors were paid at that level as well. While we welcomed the actions the company had already taken, we concluded that the resolution had merit and recommended that our clients vote in support. While the resolution did not pass, it received a good level of support from minority shareholders (over 16%), signalling the ongoing importance of this issue in the context of the UK's rising cost of living.

We asked Industria de Diseno Textil about its approach to compensation for workers. It confirmed its support for paying the living wage, the United Nations Global Compact and the Global Framework Agreement of workers' rights established by IndustriALL Global Union. We pressed the company to consider obtaining accreditation to demonstrate its commitment to meeting employee needs.

[15] Anker & Anker, Living Wages Around the World, Edward Elgar Publishing 2017

Responding to the Russia-Ukraine war



Following Russia's invasion of Ukraine in February 2022, we engaged with non-Russian companies to learn more about their response. Kenny Tsang explains what we asked companies to do and summarises our key findings.

Russia's invasion of its neighbour Ukraine has devastated cities and displaced a large swathe of the population. Alongside the tragic loss of life, the war delivered a huge shock to commodity markets due to trade disruption. This led to a surge in food and fuel price inflation, with a direct impact on families beyond Ukraine, which is still being felt.

Respect for human and labour rights is a priority engagement theme for EOS. Following the outbreak of the conflict, we temporarily suspended engagement with five Russia-listed companies and two companies with the majority of their operations and assets in Russia, as we believed it was highly unlikely they would engage with us meaningfully at that time. These included Gazprom, Lukoil and Sberbank.

Ahead of the Russian annual shareholder meeting season, we also took the decision to temporarily cease making voting recommendations and facilitating voting execution services in respect of all Russian companies. We review these decisions on an ongoing basis. We also contacted non-Russian companies in our engagement programme with material connections to Russian clients, suppliers, or counterparties.

We asked what actions they were taking to ensure the safety of employees and their families, whether they were being evacuated, and if salaries continued to be paid. We sought information on a company's increased due diligence to identify any connection to human rights violations, and the actions taken to remedy these. This should include the urgent mapping of supply chains or partners that could be involved in supporting the conflict through their products, services or finance. We also reminded companies to evaluate the risks associated with their ongoing operations and the Russia-Ukraine war, given the various sanctions imposed by Western governments that targeted Russian banks, individuals and businesses.[1]

Due to the human rights risks inherent in armed conflict, we began engaging on this issue before sanctions were announced, in the knowledge that these were likely to impact companies later. Some companies were quick to announce that they would cease operations in Russia, but withdrawing from Russia has proven difficult for those with sizeable assets there, such as oil and gas producers, for example.

> **Respect for human and labour rights is a priority engagement theme for EOS.**

How companies responded

We contacted 118 companies in the month after Russia's invasion, and by May, 87 had responded, either via email or through voice engagement. Some 55% had a connection with Russia, and 73% of these said that they had severed this connection or had taken steps to support Ukraine. Among the others who responded, 40% said that they had very limited or no material connections to Russia, and only 5% were unwilling or unable to give a clear position.

Some companies were open and transparent, and made clear public disclosures, while others were transparent in engagement but made no public statement. However, this may have been because they lacked a complete picture of their supply chains within Russia.

Kenny Tsang
Sector lead: Consumer Goods

[1] https://en.wikipedia.org/wiki/International_sanctions_during_the_2022_Russian_invasion_of_Ukraine#:~:text=After%20Russia%20invaded%20Ukraine%20on,engaged%20in%20sanctions%20against%20Russia

Cessation of operations

The energy sector was among the most exposed to criticism, as a surge in oil and gas prices following the Russian invasion swelled company coffers while putting the squeeze on household budgets across Europe. BP,[2] Shell[3] and ExxonMobil,[4] which all have joint ventures in Russia, said they would seek to exit, and their directors stepped down from the boards of their joint venture companies. BP wrote off its investment in Rosneft[5] while Exxon confirmed in October that it had exited completely after Russia seized its assets.[6]

In March TotalEnergies said it had initiated the "gradual suspension" of its activities,[7] but in October stated that it would continue to ship from its Yamal LNG plant as long as there were no EU sanctions on Russian gas.[8] In early December, the company said it had withdrawn its directors from the board of its Yamal LNG partner Novatek, in which it owned a 19.4% stake. It also took a $3.7bn write down on this stake.[9, 10]

> **We engaged with AbbVie, which said that it was monitoring the safety of its employees in the region, helping them to flee if this was possible, and if not, making sure that they had basic essentials.**

In contrast, Chinese state-owned enterprises, particularly those in the oil and gas sector, have made no public statements. Given this, and their non-responsiveness to engagement, it is possible that some will be continuing to operate in Russia.

In the retail and consumer sectors, companies such as Netflix, Sony, Nike, Amazon and Panasonic sought to temporarily suspend their services or reduce their exposure in Russia, closing stores or exiting fully. Some companies continued operating to maintain a supply of essential products. For example, Nestlé continued to supply baby food while AbbVie supplied essential medicines, while stating that it would donate any profits from these sales to support direct humanitarian relief efforts in Ukraine.[11] We engaged with AbbVie, which said that it was monitoring the safety of its employees in the region, helping them to flee if this was possible, and if not, making sure that they had basic essentials. Some companies, including Visa, worked with Russian employees who wished to explore the possibility of taking a role in other locations across the globe.

> **Some companies continued operating to maintain a supply of essential products.**

Measures to support Ukrainian employees and citizens

Companies operating in Ukraine took various steps to support their staff during the invasion, and employee safety was a topic we raised in engagements. For example, Panasonic evacuated its local employees from Ukraine to Poland or other countries, and provided food and shelter. Other companies that provided assistance to their staff included Shell and Naspers, while BASF and Nestlé offered workers in their Ukrainian operations salaries in advance, and support to relocate.[12]

Veon, which operates Ukraine's biggest mobile network, has tried to maintain a service there since the war began, with several initiatives to help Ukrainian citizens. These include free switching between mobile networks and access to services for customers who have no funds in their account. Meanwhile, some banks have offered free wire transfers.

[2] https://www.reuters.com/business/energy/britains-bp-says-exit-stake-russian-oil-giant-rosneft-2022-02-27/
[3] https://www.reuters.com/business/energy/shell-exit-russia-operations-after-ukraine-invasion-2022-02-28/
[4] https://www.reuters.com/business/energy/exxon-mobil-begins-removing-us-employees-its-russian-oil-gas-operations-2022-03-01/
[5] https://www.nytimes.com/2022/05/03/business/bp-profits-russia.html#:~:text=the%20main%20story-,BP%20writes%20off%20%2425.5%20billion%20on%20its%20Russia%20pullout%2C%20but,doubled%20from%20a%20year%20earlier
[6] https://www.reuters.com/business/energy/exclusive-exxon-exits-russia-empty-handed-with-oil-project-unilaterally-2022-10-17/#:~:text=HOUSTON%2C%20Oct%2017%20(Reuters),in%20a%20major%20oil%20project
[7] https://totalenergies.com/media/news/press-releases/russia-totalenergies-shares-its-principles-conduct
[8] https://totalenergies.com/media/news/press-releases/russia-totalenergies-continues-implement-its-principles-conduct-and-sells
[9] https://totalenergies.com/media/news/press-releases/russia-totalenergies-decides-withdraw-its-directors-novatek-and-will-no
[10] https://www.ft.com/content/2a3adda6-fe0c-4722-93fa-1ecd4498b5d6
[11] https://news.abbvie.com/news/media-statements/abbvie-will-donate-profits-from-russia-to-humanitarian-relief-efforts.htm
[12] https://www.nestle.com/ask-nestle/our-company/answers/nestle-support-ukraine

Q&A: Digital Rights

Nick Pelosi
Theme co-lead: Human and Labour Rights

Since the early days of the dotcom boom, the tech sector has expanded rapidly to create today's global platforms. These provide users with instant access to information and time-saving services, enhancing living standards. But alongside consumer benefits such as online shopping, fitness apps, informative podcasts and entertainment streaming services, the tech sector has also led to unanticipated harms and new challenges. These include the spread of hate speech, false or misleading information, and violent, racist, or extremist content on social media.

Companies must balance the right to freedom of expression with obligations to remove problematic content as well as government demands, laws, and regulations imposing censorship. In addition, the commoditisation of data creates risks to privacy rights, which may be infringed upon by governments, hackers, or companies themselves.

We have engaged with companies on digital rights and responsibilities since 2016, and in 2022 we published our Digital Rights Principles[1] to provide an engagement framework for investors in the tech sector and other data-reliant sectors.

Q. Why is this an important topic?

A. Companies whose business models misalign with best practices can have salient adverse impacts on peoples' lives while exposing their investors to material financial risks. Regulators and policymakers have scrutinised the tech sector and tightened legal frameworks in response to the social harms that have been identified.

The EU General Data Protection Regulation (GDPR) came into effect in 2016, and in 2022 the EU passed the Digital Markets Act and Digital Services Act, which aim to create a safer space for digital rights. Other emerging legal frameworks include the California Age-Appropriate Design Code Act, Canada's Digital Charter Implementation Act, and China's Personal Information Protection Law.

Companies will also be impacted by consumer preferences, disruptive technologies, and reputational risks. For example, in 2022 Meta reported significant earnings losses that were largely attributed to new privacy control features introduced by Apple. Later that year, a UK coroner found that harmful online content had contributed to the death of a 14-year-old schoolgirl in a "more than minimal way".[2] Building user trust in the protection of digital rights has become a critical part of any company's social licence to operate.

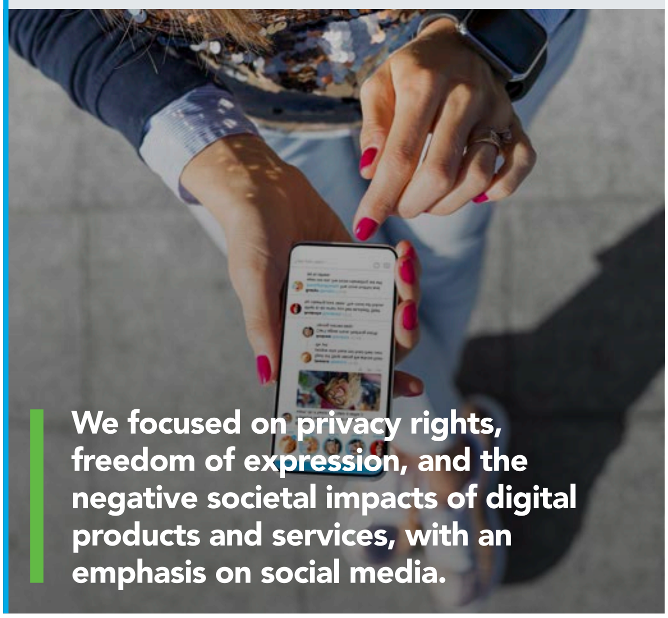
Q. What were some of the key focus areas in the Digital Rights Principles?

A. We focused on privacy rights, freedom of expression, and the negative societal impacts of digital products and services, with an emphasis on social media. These include the potential misuse of artificial intelligence (AI) for the purpose of curating, ranking, and recommending online content, physical and mental health and safety impacts on children and teens, and the growing digital divide between those who do and do not have access to technology. Companies should acknowledge where their business models contribute to negative social impacts, and cede the appropriate authority to regulators.

Q. How did we use the principles in our engagements with companies?

A. We sent letters to some of the largest tech companies around the globe including Alibaba, Alphabet, Amazon, Apple, Baidu, Kakao, Meta, Microsoft, Tencent, and Twitter, introducing the Digital Rights Principles. We made several requests including that companies obtain consent from users for the collection, inference, sharing, and retention of their data, and enhance their disclosure on enforcement of policies and protections for children and young people.

We also asked that they build trust in their use of AI, especially for the purposes of curating, ranking, and recommending online content, complete human rights impact assessments for the metaverse, and strive for leadership on other digital rights issues including content moderation, freedom of expression, and privacy rights. We met with most of these companies to reiterate these requests and track their responses.



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[1] https://www.hermes-investment.com/uploads/2022/04/5a8aadeb037fb131b1889c3f6b1a85aa/eos-corporate-digital-rights-principles-04-2022.pdf
[2] https://www.theguardian.com/uk-news/2022/sep/30/molly-russell-died-while-suffering-negative-effects-of-online-content-rules-coroner

Q. Can you give some examples of engagement outcomes?

A. We have engaged with Meta on digital rights since the 2018 Cambridge Analytica scandal in which millions of users had their data collected for political purposes without their consent. In 2022, the company published its first human rights report. The report provides some helpful information on its policies and procedures - for example, those enforcing the community standards governing content on its platforms.

However, we remain concerned that the business model, which correlates higher revenue with higher quantities of clicks, likes, posts, and shares, contributes to the spread of problematic content on its platforms. The report falls short of the highest standard for user privacy rights in our view, which is a commitment to obtaining user consent for collection, inference, sharing, and retention of their data.

Tencent made improvements to its privacy and security disclosures, but we suggested that it could offer more explicit information about user surveillance via methods including big data and AI.

We have also engaged with Tencent and Alibaba on complying with China's Personal Information Protection Law, establishing more transparent data policies, and having mechanisms in place to mitigate customer grievances. Tencent made improvements to its privacy and security disclosures, but we suggested that it could offer more explicit information about user surveillance via methods including big data and AI. We also asked for more transparency on how the company implements and monitors privacy policies in offshore jurisdictions where local laws and regulations differ from Chinese legal standards.

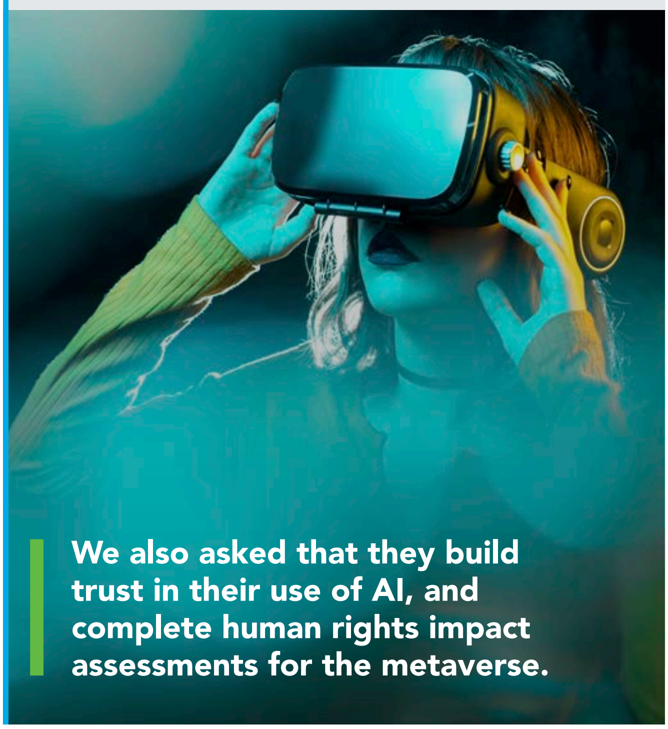
We will continue engaging on digital rights with some of the largest tech companies and tracking their responses to our requests, while expanding discussions with other sectors such as financial services and healthcare.

At our meeting with Alibaba, the company acknowledged the need to enhance its focus on ESG issues, and outlined plans to recruit experts and develop an ESG strategy that includes the responsible deployment of AI.

Finally, we engaged with standards-setting organisations for digital rights such as the Global Network Initiative and the Ranking Digital Rights Index to influence their standards and inform our views on best practice. We gave feedback on the Value Reporting Foundation's (formerly the Sustainability Accounting Standards Board's) draft reporting framework for content governance and freedom of expression, to encourage the inclusion of metrics on children and teens. We also signed a statement in support of the EU Digital Markets Act and Digital Services Act.

Q. What is our focus for 2023?

A. We will continue engaging on digital rights with some of the largest tech companies and tracking their responses to our requests, while expanding discussions with other sectors such as financial services and healthcare. We will use the Digital Rights Principles to inform our voting recommendations at relevant shareholder resolutions with companies. And we will continue liaising with the Global Network Initiative and the Ranking Digital Rights Index to advance respect for digital rights.



Engaging for impact: stewardship and society

Our conduct, culture and ethics theme was recently reorganised to reflect the wider societal impacts of positive ethical behaviours, such as zero tolerance of bribery and corruption, or the benefits of safer products and responsible tax practices. Michael Yamoah explains what this meant for our engagements.

Companies that create positive societal impacts and minimise harms will enhance the robustness of the socio-economic system upon which their financial health ultimately depends. As a consequence, we regard such companies as better stewards of investor assets over the long term. Stakeholders, including investors, consumers and regulators, are increasingly focused on how the activities, products, and services of companies could impact society at large. This is reflected in the scale of ESG assessments, which has increased in breadth and depth over the years.

Although most companies recognise well-defined environmental and social impacts, such as human rights and climate change, other societal impacts go beyond this. As businesses ultimately exist to meet the needs of society, we strongly believe that companies can only create and preserve long-term value when their activities, goods and services cause no harm, when they operate fairly and responsibly, and when they remain conscious of their ethical obligations. This is important because companies do not exist in a vacuum. Therefore, it is worth appreciating the extent to which their activities could impact a person's life and livelihood.

Through our engagements, we have advocated for companies to carefully monitor the impact of their operations, products, and services on society by:

- Eliminating bribery and corrupt practices across the value chain, as they can be damaging to communities and erode trust in institutions while undermining investor confidence. We expect boards to take responsibility for the ethical culture of a company and demonstrate zero tolerance of bribery and corruption.
- Adopting responsible tax practices with greater alignment between the tax paid and economic activity over time, and having a transparent tax policy and reporting, preferably under the Global Reporting Initiative's 207 tax criteria, with board level oversight of tax risk and controls, including at the country level.
- Ensuring that their products and services do not cause avoidable harm through improved mental and physical health and safety features as well as responsible sales and advertising practices. We expect companies to remain vigilant and conscious of the safety of their products and to be equally mindful of how they sell or advertise such products and services.
- Demonstrating ethical behaviours by eliminating damaging company practices that perpetuate inequities in society. We expect boards to underpin their internal behaviours, such as human capital policies – including those addressing diversity and inclusion – with an external lens for the impacts on society. Companies can leverage the UN Sustainable Development Goals, and systematically integrate them into their overall business strategy and operations, to help reduce potential unethical and irresponsible business practices that exacerbate social inequalities.

Michael Yamoah
Theme co-lead:
Wider Societal Impacts

Engagement highlights

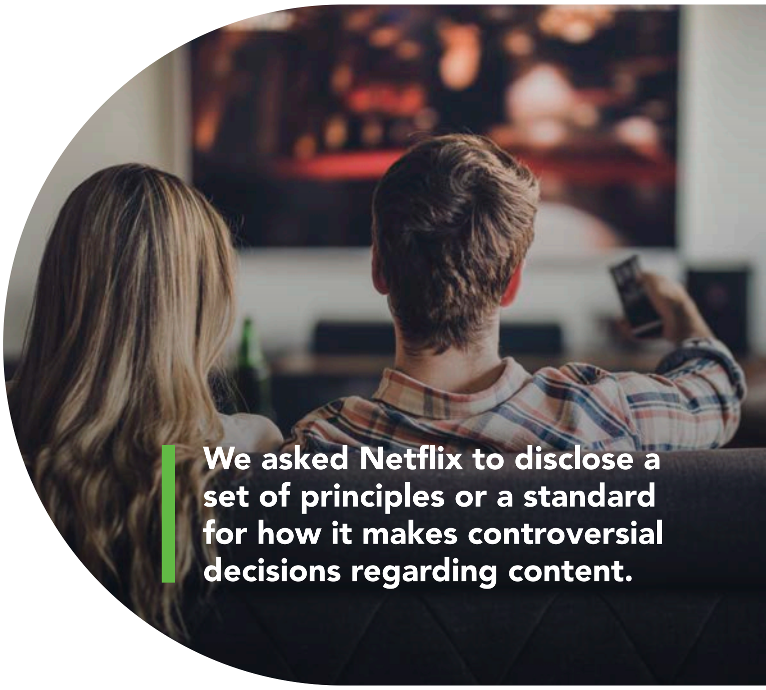
Responsible tax practices

We engaged with Amazon in 2022, ahead of the company's annual meeting, on a shareholder proposal that publicly highlighted the company's tax avoidance strategies. An exempt solicitation filed with the Securities and Exchange Commission by co-filers Pensions & Investment Research Consultants (PIRC), OIP Trust and Greater Manchester Pension Fund, stated that Amazon does not disclose revenues, profits, or tax payments in non-US markets in its standard reporting and has faced increased attention from tax authorities.[1] With management opposing the proposal it was defeated, although according to our calculations it gained a respectable 17.5% support.[2]

Microsoft, together with Cisco, faced a similar shareholder proposal for tax transparency at its 2022 annual meeting. According to the proponents, profit shifting by companies is estimated to cost the US government $70-100bn annually,[3] and the OECD estimates global revenue losses of $100-$240bn.[4] The proponents asked the company for more disclosure in line with the Global Reporting Initiative (GRI) tax criteria 207, which is in line with our engagement approach on tax.

We engaged with both companies on their tax practices ahead of the annual meeting. We urged them to provide clearer principles on responsible tax practices in line with the location of the economic value generated, and with the legislative intention of tax laws, as well as improved transparency in line with the GRI tax criteria.

Other examples include Marathon Oil, where we encouraged the company to publish the taxes it pays in Equatorial Guinea in line with the standards of the Extractive Industries Transparency Initiative (EITI). Rio Tinto already publishes reports on annual taxes paid with lump sums at the country level as well as giving the aggregated disclosure. This level of disclosure is key to ensuring that companies demonstrate their long-term social licence to operate, empowering communities to make informed decisions about the resource extraction in their backyards.



Safe products and services

Following several years of unresponsiveness, we were successful in engaging with Mattel regarding product quality and safety concerns after reports of infants dying in the company's inclined sleeper products.[5] While the company's ownership of the issue falls below our expectations, we welcomed a number of positive steps. These included removing all inclined sleepers from sale, plus the removal of any higher-risk infant toys from the market such as rockers, swings and bouncers by January 2023.

> **Following several years of unresponsiveness, we were successful in engaging with Mattel regarding product quality and safety concerns after reports of infants dying in the company's inclined sleeper products.**

Mattel also aims to improve its design controls for future products, including the use of artificial intelligence and other advanced technologies. The company is working to tackle challenges presented by the second-hand market, given the longevity of its products. With age, these products may pass through multiple households without their original product packaging and safety labels.

We engaged with Netflix to disclose a set of principles or a standard for how it makes controversial decisions regarding content. The company is mindful of ethical content and privacy concerns from customers and discloses content takedown requests. We have asked it to publish its broad approach and escalation process to executives for sensitive content. It has appointed a privacy officer and is currently considering the need for privacy reports.

[1] Microsoft Word - Exempt Solicitation Amazon 2022-04-14 (cictar.org)
[2] 0001104659-22-065872 (d18rn0p25nwr6d.cloudfront.net)
[3] https://microsoft.gcs-web.com/static-files/feb8500e-842e-45b2-b0cf-82ff26b34e3d
[4] https://microsoft.gcs-web.com/static-files/feb8500e-842e-45b2-b0cf-82ff26b34e3d
[5] https://www.consumerreports.org/baby-product-recalls/deaths-linked-to-fisher-price-rock-n-play-after-recall-a1183945428/

Bribery and corruption

We have engaged with commodity trading house and mining company Glencore, which pleaded guilty to charges of bribery and corruption with criminal and civil authorities in the US, UK and Brazil.[6] The company admitted to providing payments and bribes via third parties acting on its behalf to foreign officials in Nigeria, Cameroon, Ivory Coast, Equatorial Guinea, Brazil, Venezuela, and the Democratic Republic of the Congo (DRC).[7]

We engaged with the chair of Glencore to identify key learnings for the company on ethical culture and behaviours, and to develop a plan to address them. We have been assured that it has taken remediation action, including appointing a new chief compliance officer, refreshing the management team and CEO, and reporting to the board on compliance on a quarterly basis. A court-appointed monitor of its compliance programme is in place for the next three years.

> **We engaged with the chair of Glencore to identify key learnings for the company on ethical culture and behaviours, and to develop a plan to address them.**

Teva Pharmaceutical Industries was rated as non-compliant with regard to the UN Global Compact on business ethics. We have engaged the company on its actions to improve its business ethics and due diligence since 2017. During engagement in 2022, the company noted that it takes a risk-based approach to compliance training with sales employees and senior leaders receiving additional training due to their role. It acknowledged that it could provide more disclosures on what the training covers. We welcomed the company's use of a third-party survey to assess its culture of compliance.

Ethically responsible

We have engaged with the Walt Disney Company, which has recognised the need to amplify under-represented voices, and the importance of accurate representation in media and entertainment. The company has created two senior leadership councils focused on DEI in the workforce and content. We also welcomed the company's intention to advance representation for people of colour and other diverse groups in front of and behind the camera. We see this in its film Encanto, which depicts a Colombian family. We encouraged the company to set and disclose qualitative and quantitative DEI goals, and we expect its content representation dashboard to provide a baseline to support this.

The CEO and the board have regular oversight of its **244** point improvement plan and the CEO has been leading work on the desired culture for the bank.

We encouraged Swedbank to develop a robust anti-money laundering (AML) policy and procedures with oversight by the board. The company acknowledged a commitment to align to best practice with its Scandinavian peers and Europe. The CEO and the board have regular oversight of its 244-point improvement plan to address AML protections, and the CEO has been leading work on the desired culture for the bank. It has completed more than 90% of its action plan and the remaining measures have been transferred to the bank's change programme. We see improvements but continue to press for more granular disclosure in its reporting, and concrete examples of actions taken and targets.

> **We encouraged the company to set and disclose DEI goals, and we expect its content representation dashboard to provide a baseline to support this.**

[6] https://www.justice.gov/usao-sdny/pr/glencore-entered-guilty-pleas-foreign-bribery-and-market-manipulation-conspiracies

[7] https://www.justice.gov/opa/pr/glencore-entered-guilty-pleas-foreign-bribery-and-market-manipulation-schemes "Glencore Entered Guilty Pleas to Foreign Bribery and Market Manipulation Schemes | OPA | Department of Justice

Sexual harassment and discrimination

In 2022 we engaged with several companies on their culture as part of our human capital theme work, following worrying reports of sexual harassment and discrimination. Emily DeMasi outlines these cases and what we asked companies to do.

To tackle gender issues effectively in the workplace, companies must address them at the highest level, creating a culture of safety and inclusion for all their workers. The importance of this was underscored in 2022 by disturbing reports of sexual harassment in two traditionally male-dominated industries – mining and video games.

We believe that companies mired in such issues should disclose their strategy for addressing the problem to their stakeholders, and report regularly on their actions and progress. A failure to do so could trigger further controversy, heighten reputational risk, and impact business strategy, as some companies discovered in 2022.

Mining

Following the Australian Human Rights Commission report[1] showing that 74% of women in the mining industry had experienced some form of sexual harassment in the past five years, we decided to focus on sexual harassment in our engagement with BHP. An investigation into the 'fly-in, fly-out' mining industry in Australia had uncovered some shocking cases.[2] These sites are often extremely isolated, with the predominantly male workers housed in camps, and a culture of hard drinking.[3] Women are extremely vulnerable in these situations.

We participated in BHP's investor briefing on social values in Q2 2022, with its external affairs officer. We asked if BHP would disclose the results of its workforce survey on sexual harassment and explain how this had influenced its strategy. The company said that a sexual harassment metric was now included in remuneration schemes and that it would provide more information on issues and remediation actions in its next report.

We asked if BHP would disclose the results of its workforce survey on sexual harassment and explain how this had influenced its strategy.

In a meeting with the remuneration committee chair in Q2 2022, we asked if sexual harassment was properly reflected in BHP's remuneration. BHP said that sexual harassment was integrated into remuneration through the health, safety, environment and community metric that forms 25% of its short-term incentive plan.

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We gained reassurance that sexual harassment was an issue that was addressed at board level, and that BHP was working to implement some measurable improvements. These included increasing lighting and telephones on sites and reducing the consumption of alcohol in mining camps.

Emily DeMasi
Theme co-lead: Human Capital

[1] https://humanrights.gov.au/our-work/sex-discrimination/publications/respectwork-sexual-harassment-national-inquiry-report-2020

[2] https://www.parliament.wa.gov.au/Parliament/commit.nsf/(Report+Lookup+by+Com+ID)/EF1DF1A3F5DF74A848258869000E6B32/$file/20220621%20-Report%20No%202.pdf

[3] https://www.bbc.co.uk/news/world-australia-61906057

In BHP's 2022 report, it provided improved disclosure around sexual harassment including the number and type of incidents. We were pleased with this progress and in a call with the chair of the remuneration committee in Q4 2022, we encouraged BHP to continue its efforts, for example by disclosing the results of its employee survey. BHP has a global target of 50% female representation by 2025, and is hiring and training more women. The hope is that this will help to eliminate sexual harassment. We will continue to monitor the company's progress.

Video games

The video game industry already had a poor reputation for its lack of inclusivity[4] but this was reinforced by lawsuits brought against US gaming company Activision Blizzard, which resulted in multi-million dollar settlements.[5] We conveyed our concerns to the company after allegations of sexual harassment and discrimination, and expressed our disappointment in the response from its CEO and the board. In our view, the public communication and commitments made did not reflect the seriousness of the matter, nor did they address the various material short and long-term risks for the company and its shareholders.

We first raised these concerns in Q4 2021 with the head of investor relations who pointed to changes enacted by the company in the wake of media reports. These measures included increasing diversity, conducting an equity pay gap analysis, increasing hourly wages for part-time employees and instituting a workplace responsibility committee. We pointed out that most of these changes were target-related and while laudable, did not address the root cause of the problem, which appeared to be one of culture.

We followed up this meeting with a formal letter to the board setting out our expectations around board governance of sexual harassment and discrimination issues. We also posed some detailed questions for the company to address in a subsequent meeting with the lead independent director or co-chairs of the workplace responsibility committee. Four months later, the vice president of ESG and shareholder outreach sent a reply, outlining the board's approach to some of the issues we had raised. We found this response to be insufficient, and our request for a meeting went unanswered.

At the company's 2022 annual meeting, we recommended support for two shareholder proposals that could help Activision Blizzard improve its management of human capital, human rights and the associated risks following the sexual harassment and discrimination allegations. The first proposal asked for a report on the company's efforts to prevent abuse, harassment and discrimination. The second urged the board to adopt a policy of nominating a director candidate selected by the company's non-management employees. We agreed with the latter's proponents that an employee representative on Activision's board would be particularly beneficial given the allegations and the lack of an appropriate response from the company.

Technology

Tech giant Microsoft found its own culture under scrutiny when it announced plans to buy Activision Blizzard in January 2022. In Q1 2022 we engaged with Microsoft on a 2021 shareholder proposal that had gained 78% support, asking the board to report on the effectiveness of its workplace sexual harassment policies.

The company said that its communications on these issues had improved. It also committed to annual public reporting on the implementation of its sexual harassment and gender discrimination policies, including the total number of reported concerns, the percentage substantiated and the types of corrective actions taken. We appreciated this transparency and encouraged it to integrate its policies and practices at Activision Blizzard when the acquisition closed.

We forwarded to Microsoft our expectations for board oversight of sexual harassment and discrimination issues that we had sent to the Activision board. We were pleased to receive Microsoft's first report on its workplace culture with an independent review via email in late 2022.

In Q1 2022 we engaged with Microsoft on a 2021 shareholder proposal that had gained

78%

support, asking the board to report on the effectiveness of its workplace sexual harassment policies.

We will continue to engage with these companies on their approach to gender equity, governance of sexual harassment and discrimination, and a culture of safety for women, and all employees. In 2023, we will intensify our engagement with these sectors and look to broaden our approach to others where there may be similar systemic problems, particularly where women are historically under-represented and therefore may be more at risk.

[4] https://www.theguardian.com/technology/2021/aug/08/activision-blizzard-lawsuit-women-sexual-harassment
[5] https://www.theguardian.com/technology/2022/mar/29/activision-blizzard-sexual-harassment-lawsuit-eeoc-settlement

CASE STUDY

Starbucks

At coffee chain Starbucks, we were concerned that the company's anti-bias efforts had stalled since its initial 2018 US-wide training session, which followed the unjustifiable arrest of two African-American men in one Philadelphia store.[1]

In 2020 we raised our human rights-related concerns with Starbucks' director of global compliance and international markets. We said that there had been no attempt to measure the impact of its anti-bias training in terms of whether African-American and other ethnic minority customers now felt safer in its stores. Also, it did not seem as if there had been attempts to build on and repeat the training, except for new starters. The company had realised that the US-focused training had not worked in Canada, and it had postponed the roll out of the training internationally, while acknowledging that racism was an issue.

In 2021, we met the chief inclusion and diversity officer and his team, who responded to our questions on the impact of the anti-bias training and its global inclusion and diversity strategy.

Starbucks appointed a chief inclusion and diversity officer in 2020 and expanded its inclusion and diversity strategy in 2021, which mandated its anti-bias training for vice president level and above. In 2021, we met the chief inclusion and diversity officer and his team, who responded to our questions on the impact of the anti-bias training and its global inclusion and diversity strategy.

The chief inclusion and diversity officer confirmed that the company had considered the experiences of racially-diverse customers by collecting feedback from external civil rights groups as a proxy for customer experience. It had also taken feedback from customer helplines. Managers were expected to respond to concerns raised by partners (employees) through anti-bias questions in the annual partner survey.

Starbucks said that it would continue to explore mandating training for all partners, while tracking enrolment and completion rates for an expanded version of the training.

Starbucks said that it would continue to explore mandating training for all partners, while tracking enrolment and completion rates for an expanded version of the training. Additionally, we welcomed the company's commissioned Civil Rights Assessment, conducted by a third party annually since 2019. The company also expressed a commitment to sustaining a Third Place where everyone should feel welcome.

With Starbucks' union negotiations ongoing in 2022, our human rights engagement focus changed. We encouraged the company to acknowledge and respond to concerns about worker rights by reporting on the number of employee and supplier grievances received and remedied, and to pay a living wage or its equivalent.

Velika Talyarkhan
Theme lead:
Executive Remuneration

[1] https://www.theguardian.com/business/2018/apr/19/starbucks-black-men-feared-for-lives-philadelphia

Governance

Strain on social contract spurs rise in shareholder proposals

Shareholder resolutions on social issues were in the spotlight during the 2022 voting season, as soaring inflation eroded the purchasing power of wages. Meanwhile, say-on-climate votes went mainstream as more companies asked investors to approve their transition plans.

The 2022 shareholder meeting season saw social issues rise up the agenda with resolutions on everything from animal welfare to paid sick leave and reproductive rights. Meanwhile, as soaring inflation eroded the purchasing power of take-home pay, investors pressed for living wages for struggling workers. It was also the second year for formal shareholder votes on companies' responses to climate change, with a steep rise in management say-on-climate proposals, and new votes at BP, Anglo American and Rio Tinto. Shell and TotalEnergies also offered a chance to vote on the progress achieved since the 2021 proxy season.

In 2022, we made voting recommendations at 13,814 meetings, covering 134,188 proposed resolutions. This was up from 13,412 meetings in 2021 and 128,858 proposed resolutions. Overall, we made at least one voting recommendation against management at 66% of meetings, versus 63% in 2021. For North America we recommended against management on 6,839 proposals, or 22%, versus 23% in 2021. We 'attended' 13 shareholder meetings and asked questions at eight of these, including BP, Volkswagen, BMW, Royal Bank of Canada, Bank of Nova Scotia, Siemens Energy and Canadian Imperial Bank of Commerce. At Berkshire Hathaway we made a statement and co-filed a shareholder resolution.

Climate change

Climate voting gained momentum in 2022 following its debut in 2021. We provided recommendations on 58 say-on-climate proposals from management teams, asking investors to approve transition plans or providing an annual update on already-approved plans. We also started to assess the integration of climate-related considerations into some companies' financial accounts and audit practices. We expanded our proactive vote policy, which has been in place for four years and targets laggard companies that are

In 2022 we recommended votes for

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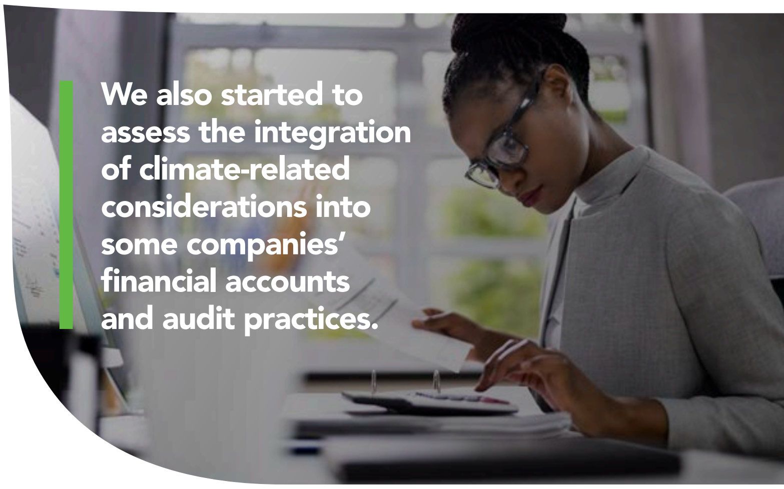
13,412 meetings in 2021.

materially misaligned with the goals of the Paris Agreement. In total, we recommended voting against directors or relevant proposals at 292 companies in 2022, up from 144 companies in 2021, due to concerns about insufficient management of climate-related risks.

We took a robust approach to assessing companies' climate transition plans, recommending voting in favour of those we believed were substantially aligned with 1.5°C. This included cases where the company clearly indicated that alignment was the goal, with a more developed plan to be put to a further vote, such as at NatWest and Amundi.



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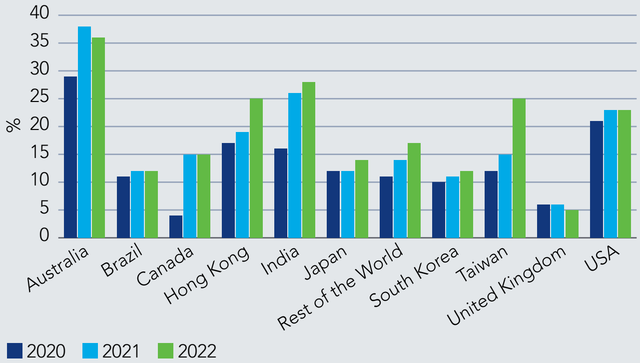
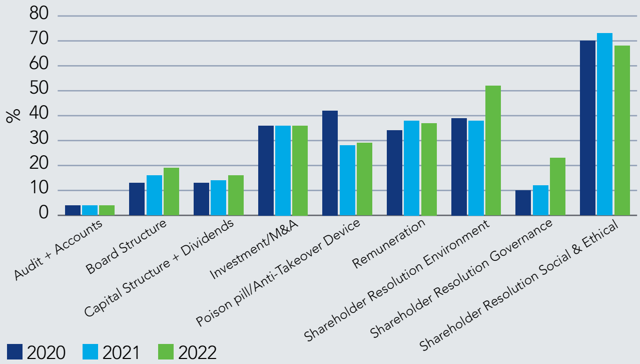
Percentage of proposals voted against management per key market 2020-2022



Proportion of resolution type with recommended votes against management



Source: EOS data

We recommended opposing the plans at Shell, TotalEnergies and Standard Chartered where climate ambition was materially below our sector-specific expectations. At Barclays and Standard Chartered, we engaged with management after identifying areas that fell below our 1.5°C-aligned expectation. Following our discussions, Barclays published a late clarification of its climate plan, emphasising its commitment to targeting 1.5°C portfolio alignment, which ultimately prompted us to recommend support. Standard Chartered failed to make further commitments to improving its coal policy or its methodology for setting decarbonisation targets, which led to us recommending a vote against its plan.

> **At Barclays and Standard Chartered, we engaged with management after identifying areas that fell below our 1.5°C-aligned expectation.**

Climate-related shareholder proposals

As well as these say-on-climate votes, many climate-related shareholder proposals were filed. Some companies supported such proposals, including one at Caterpillar for a report on long-term greenhouse gas targets aligned with the Paris Agreement, which attracted 96% support. Boeing was asked for a report on a net-zero emissions by 2050 ambition, and whether it intended to revise its policies to align with the Paris Agreement. This attracted 89% support. It was encouraging to see companies and boards supporting climate shareholder proposals and seizing the opportunity to engage with investors and their representatives, as opposed to being defensive and automatically opposing.

In Japan, NGOs and international investors flexed their muscle on climate action, filing climate-related shareholder proposals at three power utilities and two financial groups. These received strong support, topping 20% in some cases. We were active in engagement in the lead-up to the voting in each case, and at J-Power, we recommended support for all three climate-related shareholder proposals. These included aligning the 2050 business plan with the goals of the Paris Agreement, which received almost 26% support. At Tepco and Chubu Electric, we recommended support for proposals asking the companies to disclose how their energy assets would be affected by a net zero by 2050 pathway, with the Chubu proposal winning almost 20% support.

Shareholder proposals brought in previous years have subsequently influenced commitments by major Japanese banks and trading houses to pull back from financing new coal projects. At Sumitomo Mitsui Financial Group, we recommended support for one shareholder proposal asking the bank to disclose short- and medium-term emissions reduction targets and set an appropriate strategy in line with the goals of the Paris Agreement. This attracted 27% support. We also recommended support for both climate-related shareholder proposals at Mitsubishi Corp covering target-setting for emissions reductions aligned with the Paris Agreement goals, and capital expenditure alignment.

Coal and deforestation

We continued to develop our proactive climate vote policy, to identify companies whose activities are more clearly misaligned with the goals of the Paris Agreement, including through coal and deforestation. For coal exposure, we targeted companies that were expanding coal infrastructure or materially producing or deriving revenue from coal-related activities without an adequate plan for phase-out. We were supportive where we were satisfied that progress was being made. However, we had red lines on the expansion of coal-fired power or coal mining infrastructure, and opposed directors at Evergy, Sumitomo, WEC Energy Group and Mitsubishi.

For deforestation, we recommended opposing the directors responsible at companies that were the poorest performers on the Forest 500 assessment, which targets companies that are most exposed to deforestation risks. This led us to oppose the directors responsible at retailer TJX and food manufacturer Kikkoman.

Social issues proposals on the rise

In 2022 we saw record numbers of shareholder proposals at major US companies, including many on social issues, against a backdrop of soaring inflation and a tumultuous political environment. These covered topics such as paid sick leave, reproductive rights risks, unionisation, and animal welfare, some of which were supported by high-profile campaigns.

For example, at retailer TJX, we supported a shareholder proposal to adopt and publicly disclose a policy that all employees, part- and full-time, accrue some paid sick leave that can be used after working at TJX for a reasonable probationary period. The proposal garnered over 33% support showing that shareholders increasingly view paid sick leave as a basic human right.

At Meta, we used our recently published EOS Digital Rights Principles to inform our decisions and justify our support for several shareholder resolutions. These included requests for a report on the enforcement of policies to moderate problematic content; a human rights impact assessment of targeted advertising; and a report on the trade offs between privacy rights and child protection. We noted the company's willingness to engage on these issues ahead of the annual meeting, but recommended opposing the CEO and the entire governance committee due to the dual class share structure and other issues.

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More Civil Rights Audit (CRA), Racial Equity Audit (REA) and Racial Justice Audit shareholder proposals were filed this proxy season, including at Apple, Chevron, Wells Fargo and Johnson & Johnson. In general, such proposals urged boards to oversee a third-party audit analysing the adverse impacts of companies' policies and practices on the civil rights of stakeholders.

In 2022, we recommended support for the Apple CRA shareholder proposal, which received 53.6% shareholder support. Where we assessed that the intention of a proposal was to undermine racial equity, such as those at Levi Strauss, Bank of America and Citigroup, we recommended opposing.

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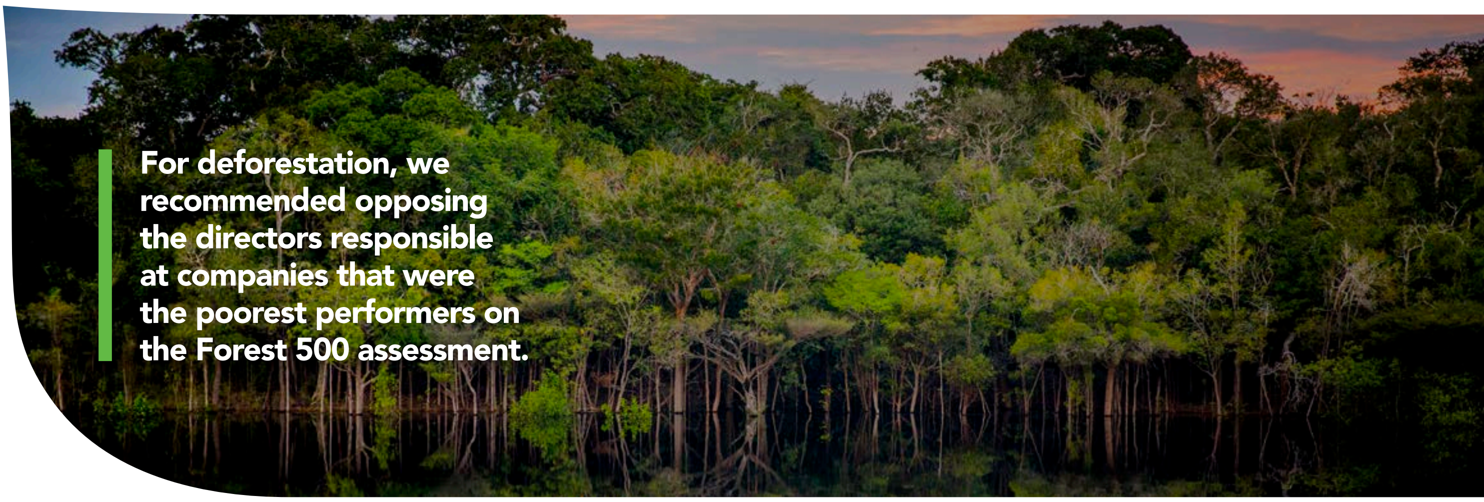
We had updated our voting policy to consider recommending votes for relevant proposals or against directors where a company was in clear breach of its applicable regulatory human rights responsibilities or those outlined in the UN Guiding Principles on Business and Human Rights. We treated 2022 as a pilot, identifying the highest-risk companies in our engagement programme and alerting them that we had updated our policy. We then recommended opposing directors on human rights grounds at a small number of companies. These included Telefonaktiebolaget LM Ericsson, due to various alleged compliance breaches and insufficient remedial actions, Grupo Mexico, due to spills of toxic waste and heavy metals in rivers adjacent to its mines, and Meta, due to the spread of problematic content on its platforms.



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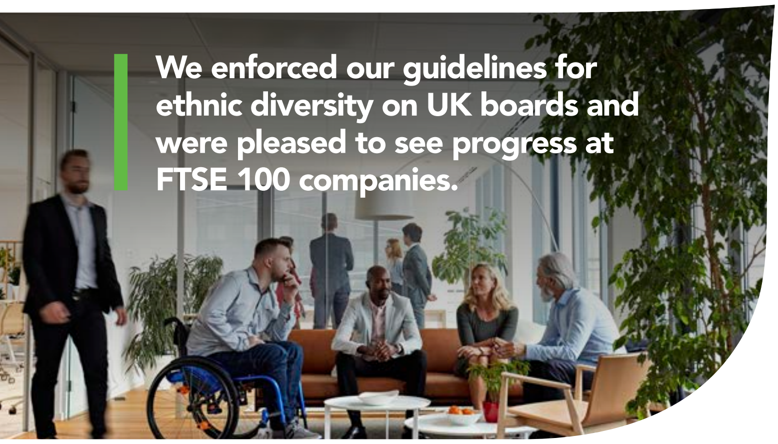

Diversity and inclusion

We again tightened our diversity and inclusion voting policies, encouraging greater representation of women and ethnic minorities on boards and in leadership teams. Globally, we recommended voting against 2,920 proposals due to diversity concerns, versus 2,693 proposals in 2021.

In the US, where we expect women and ethnic minorities to make up at least 40% of the board at the largest companies, with a minimum of 30% gender diversity in line with our support for the 30% Club, we opposed 1,033 proposals for insufficient gender and ethnic diversity. This included at Berkshire Hathaway, Amgen, United States Steel, Sinclair Broadcast Group, FreeportMcMoRan, Kinder Morgan, Dollarama and NextEra. In India we opposed 214 proposals on this issue, up from 128 in 2021.

In Europe, we continued to push for greater gender diversity on boards and in leadership teams and opposed companies that did not meet our minimum expectations. This included at miners Antofagasta, where we opposed the nomination committee chair for poor board gender diversity, and Fresnillo.

We enforced our guidelines for ethnic diversity on UK boards and were pleased to see great progress by FTSE 100 companies in meeting minimum standards of representation. We continued to oppose chairs where this was not the case, for example at DS Smith. Overall in the UK, we opposed 19 proposals for concerns about insufficient diversity, including gender diversity, at board level and below, versus 37 proposals in 2021.

The slow progress in board and senior management gender diversity in Brazil led B3, the Brazilian Stock Exchange, to propose the introduction of a new listing rule, on a comply or explain basis. This requires companies to have at least one woman and one ethnically diverse member on the board or the executive committee from 2025. This remains below our expectations, which are reflected in our voting policy.

Legal requirements are also tightening in South Korea, Malaysia and Hong Kong. In the latter, we were pleased to see progress at companies such as Geely Automobile, where board gender diversity reached 30% after several years of engagement on this topic. At AIA Group and Ping An Insurance, we recommended support for directors by exception to our policy to recognise their progress in reaching a level of diversity that is just below our minimum expectations. However, we recommended votes against at Beijing Enterprises, China Mengniu Dairy, and China Resources Beer. More focus is needed to raise female board membership far above our current 20% minimum threshold.

In Japan, there was progress on gender diversity in companies such as Chubu Electric Power and retailer Seven & i. However, other companies are lagging, including Shin-Etsu Chemical, Canon, Toyota Industries and Toray Industries, which led us to recommend votes against the responsible directors and step up engagement on gender diversity. At Chugoku Electric Power, we recommended voting for a non-executive female director, despite her long tenure, in order to achieve improved gender diversity.

Executive pay and auditor rotation

We saw a resurgence in some executive pay packages in 2022, so overall we recommended a vote against 65% of pay proposals. In North America, we continued to oppose the majority (78%) of say-on-pay proposals on the basis that practices across the region remained materially misaligned with our principles. For example, we recommended voting against executive pay and the compensation committee chair at Netflix. Some 73% of shareholders rejected the pay proposal, so we will expect a robust response from the compensation committee in the coming year.

We also recommended opposing pay at Caterpillar, Walmart, Visa, Morgan Stanley, Meta, ExxonMobil, Chevron, Mondelez International, JPMorgan Chase and many more. This was mainly for excessive quantum, without adequate disclosure of the additional value created for long-term shareholders when paying the CEO significantly above the labour-market median.

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In the UK, we opposed 17% of remuneration policy proposals versus 23% in 2021. In Europe, we pushed for greater shareholdings for executives, and improving disclosure where this was lacking or where pay awards were substantial. We scrutinised what appeared to be excessive pay levels, whether these came through salary increases or incentive scheme opportunities.

For example, at GSK we were not supportive of a remuneration policy that continues to increase the variable pay opportunity far in excess of our policy limits. We also noted a duplication of metrics across the bonus scheme and long-term incentive plan (LTIP), which we generally do not support as it rewards executives twice for the same performance.

We pushed for better auditor independence with a focus on long audit firm tenures in the US, where some have been in place for over 100 years. In 2022 we set expectations for companies to voluntarily rotate the auditor after 20 years. In the US, the rotation of the lead audit partner every five years is not sufficient to strengthen auditor firm independence in our view. Where an audit firm has been in place consecutively for more than 20 years, we will consider recommending votes against the audit committee chair and the auditor ratification.

Q&A: Key updates to voting policies and disclosure

Amy Wilson
Theme lead: Business Purpose & Strategy

Each year we update our global voting policy guidelines, which inform the recommendations we issue to our clients. For 2023, we continue to take a tailored approach to voting across the key global markets where EOS clients have holdings, setting out our broad position on a number of topics in our global voting policy. We have also outlined our market-specific voting principles and policies in our Public Vote Guidelines for Europe and North America, a new EOS publication for 2023, and our Corporate Governance Principles in Asia and Global Emerging Markets.

Q. Given that there are still significant representation gaps on company boards and executive management teams, how have we updated our voting policies for diversity?

A. We remain concerned by the slow pace of progress to address low diversity on company boards around the globe. In 2022, following an intensive review of diversity expectations, corporate governance codes, and progress across the 22 markets where we publish Corporate Governance Principles, we increased our diversity expectations in most markets in the UK, Europe, North America, Asia and emerging markets. We engaged with companies throughout 2022 on defining strategies to meaningfully address these concerns. While we will continue to push companies across most markets to meet these thresholds, we have updated a select group of our diversity policies for 2023.

In North America, we will expect companies of all sizes, not just those listed on the S&P 500, to have a minimum of 40% overall diversity. Within this, we will expect a minimum of 30% gender diversity and at least one director from a diverse racial or ethnic background. We also welcome the inclusion of directors identifying as LGBTQ+ and those with disabilities in the composition of this 40%, beyond the gender, racial and ethnic thresholds specified.

We continue to push for a minimum of **30%** women on boards and at least one woman on executive committees across Europe.

We continue to push for a minimum of 30% women on boards and at least one woman on executive committees across Europe. In the UK, we hardened board gender diversity rules to 33% women on FTSE 350 boards and endorsed new ‘comply or explain’ listing rules targets for women on boards in key positions, including chair, senior independent director, CEO and CFO, and for ethnic diversity on boards at a minimum threshold of one director.

We are introducing new policies for below board diversity and will oppose all-male executive committees across the FTSE 350 (previously this was FTSE 100 only). We expect women to account for 25% of the executive committees and direct reports of FTSE 100 companies, extending this to 20% for the FTSE 250 in 2023.

> **We remain concerned by the slow pace of progress to address low diversity on company boards around the globe.**

We expect to see new EU regulations addressing gender diversity and will review these to determine our view and how they may impact our vote policies.

We welcomed a recent update to the Malaysian Corporate Governance Code, which requires that women make up at least 30% of all boards, and have aligned our policy with this expectation, up from a 20% level in 2022. We expect a minimum of 20% women on boards across much of Asia and the global emerging markets.

In Japan, we have set a minimum of 10% for most companies but have increased our expectation for the largest companies to a minimum of two women. We consider recommending a vote against the relevant directors for inadequate disclosure of director gender identity across the region.

> **We welcomed a recent update to the Malaysian Corporate Governance Code, which requires that women make up at least 30% of all boards, and have aligned our policy with this expectation.**

Q. We introduced our human rights voting policy in 2022. How has the policy evolved since its launch?

A. In the second iteration of our human rights voting policy, we will continue to focus on companies in clear breach of regulatory responsibilities or those that have caused or contributed to egregious, adverse human rights impacts or controversies, without providing appropriate remedy. In 2023, we will also be reviewing companies scoring significantly lower than industry peers on credible external human rights benchmarks, including: the Corporate Human Rights Benchmark, the Ranking Digital Rights Index, the BankTrack Human Rights Benchmark, and the Know the Chain Index.

Q. In 2022 we saw a proliferation of votes on climate transition plans. Do we expect this to continue in 2023? Have we made any changes to our broader climate change voting policy for 2023?

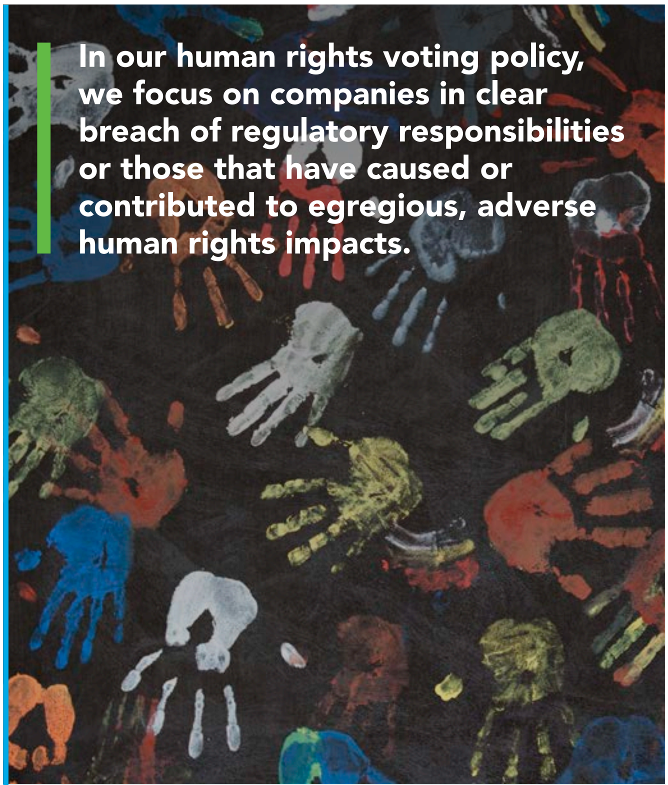
A. We expect to see an increasing number of 'say-on-climate' proposals in 2023 and will continue to assess these against the criteria of alignment with the Paris Agreement goals and limiting global warming to 1.5°C, the quality of the company's plan to deliver this, and the commitment of the company to achieving its stated goals. As good practices for these proposals develop, we may look to communicate more detailed vote policy guidelines to support their continued improvement across markets.

> **After piloting new policies to address excessive auditor tenure and non-audit fees in North America, we updated our approach for 2023, hardening our policy for tenure.**

We are also making some changes to our broader climate change voting policy, considering that 2023 will be the fourth iteration of our policy to hold the responsible director accountable when a company's strategy and/or actions are materially misaligned with the goals of the Paris Agreement and a 1.5-degree pathway. We have tightened our expectations for performance against the Transition Pathway Initiative's management quality score, and continue to inform our assessments using additional frameworks, including the Climate Action 100+ Benchmark.

Q. Remuneration continues to be an issue across most markets. Are we making any changes to our policies or how we engage around remuneration issues?

A. As well as continuing our focus on issues such as excessive variable pay and insufficient long-term share ownership for executives, in 2023 we will be assessing executive and workforce pay against a context of widening income inequality, a global cost of living crisis and an uneven post-pandemic recovery. We will expect companies to demonstrate how they provide fair, living



wages to their workforce in conjunction with good quality employment, and scrutinise any executive pay awards that appear misaligned with wider workforce pay. We will also review incentive schemes granted during the pandemic that appear to have produced undeserved windfall gains for executives as markets rebounded.

Q. Are we making any changes around audit?

A. After piloting new policies to address excessive auditor tenure and non-audit fees in North America, we have updated our approach for 2023. We have hardened our policy for tenure and will oppose ratification of the auditor and chair of the audit committee when tenure is over 100 years.

In terms of non-audit fees, we found that these fees were not as egregious as feared. Through our own research and engagement, we found that even in instances where non-audit fees were marginally higher than 15% of total fees, the audit committees had robust processes in place for reviewing and approving these fees, including an approval threshold in some instances. Also, they were often for justifiable purposes, such as to support M&A or other restructuring activities.

> **In 2023 we will be assessing executive and workforce pay against a context of widening income inequality, a global cost of living crisis and an uneven post-pandemic recovery.**

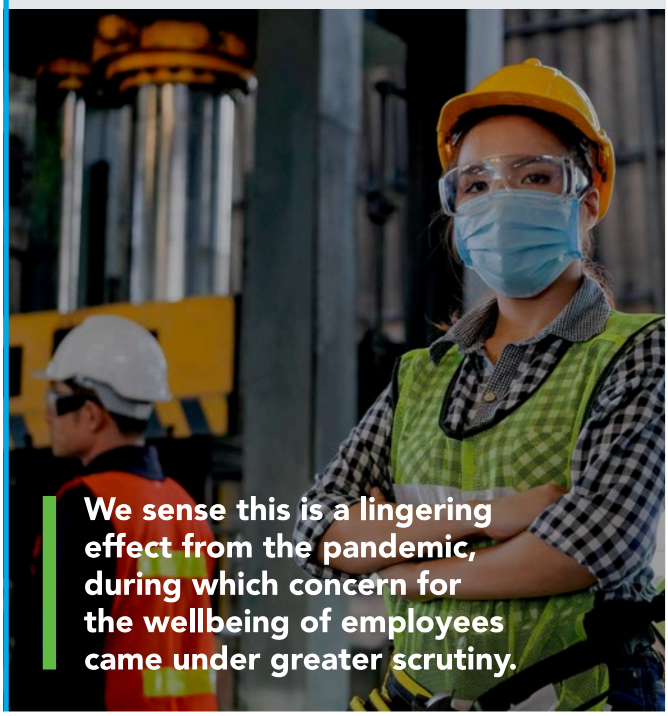
Q. Over the past couple of years we have seen growing numbers of shareholder proposals addressing environmental and social concerns across many markets. What is driving this and do we expect it to continue?

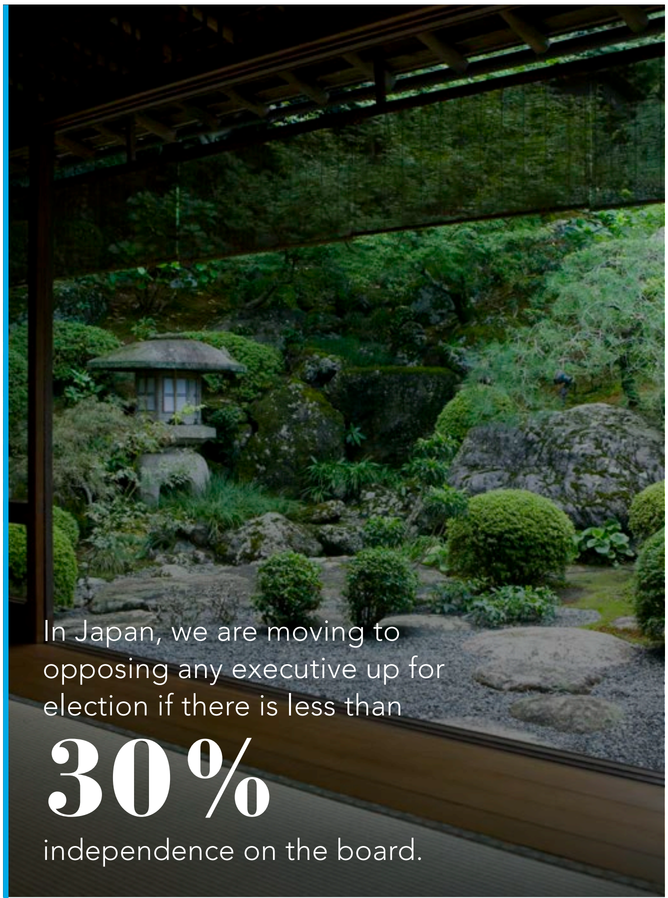
A. We have seen an overall increase in shareholder proposals covering environmental and social issues. From 2021 to 2022, the total number of these proposals increased from 308 to 447, with the majority of the proposals targeting social and ethical issues. At least part of this increase may be attributable to a rule change by the US Securities and Exchange Commission (SEC). This significantly narrowed the scope for a company to exclude shareholder proposals from the proxy statement, especially those addressing environmental and social issues including climate change and human capital management.

We also sense that this is a lingering effect from the Covid-19 pandemic, during which concern for the wellbeing of employees, and a company's actions to protect them, came under greater scrutiny. We expect this trend to continue, driven by growing investor attention focused on how companies manage environmental and social risks throughout the value chain.

Q. Are we making any other notable changes in Asia and global emerging markets (GEMs)?

A. We are taking a tougher stance on board independence in some Asian and global emerging markets, and have hardened guidelines for non-watchlist companies to oppose, rather than consider opposing a combined CEO/chair if there is no lead independent director. In Japan, we are moving to opposing any executive up for election if there is less than 30% independence on the board. Also in Japan, we are tightening the cross-shareholding voting threshold as this continues to be an issue of concern in the market.





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308 to **447**.

Q. Have we made any changes to how we communicate our expectations and voting policies?

A. We have made a shift in how we design and publish information about our voting policies and governance expectations externally. In an effort to streamline our disclosure in a way that makes it more transparent and useful for companies and clients, we have moved from publishing market-level Corporate Governance Principles to publishing regional Public Vote Guidelines in some markets.

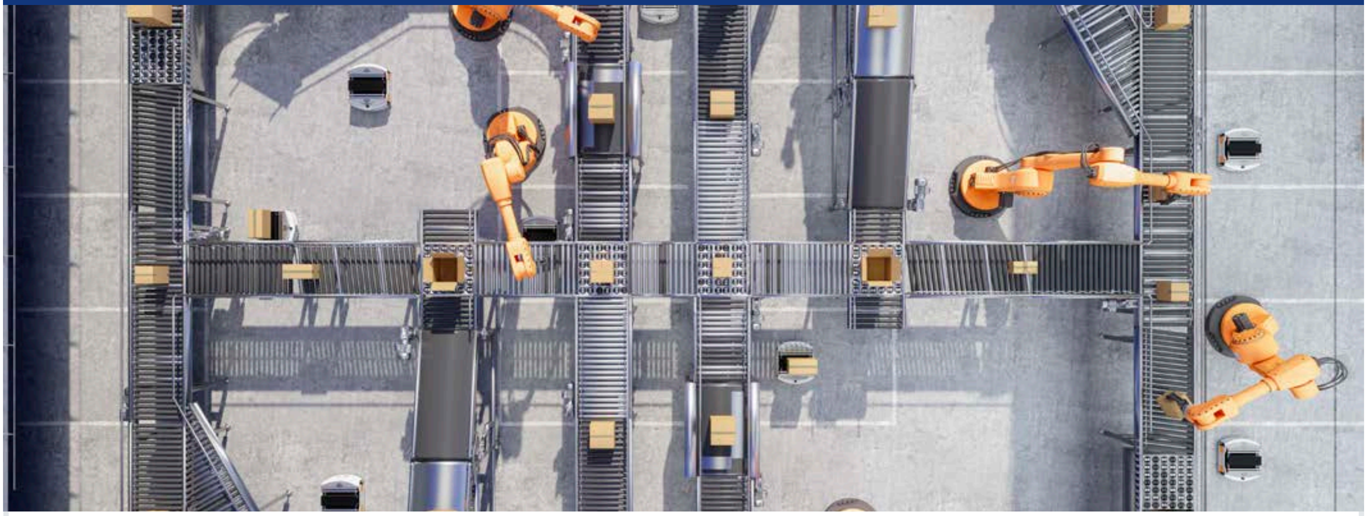
For 2023, we published Public Vote Guidelines for North America and Europe, with Asia/GEMs expected to follow in 2024. While our Corporate Governance Principles focused on the high-level principles that guided our vote policies across 22 global markets, our Public Vote Guidelines place a stronger emphasis on the policies themselves, which more directly inform the voting recommendations we issue to our clients.

We also published a set of Global Corporate Governance Principles to provide more information on what EOS considers to be governance best practices, not limited to issues with direct vote policy implications.

CASE STUDY

Alibaba

We have engaged extensively with Alibaba on a range of governance issues including board independence, as well as the need for improvements in the company's ESG strategy and reporting.



China's Alibaba provides online, offline and mobile marketplaces, alongside other services such as cloud computing and digital media and entertainment, both in China and internationally. It is dual-listed in the US and Hong Kong, with overseas investors accessing the stock via a variable interest entity structure (VIE). Initially, little information was provided about the governance, the appointed directors and the oversight of this entity, or how it interacted with the Hong Kong-listed company.

In addition, Alibaba has a partnership structure, raising concerns about board and committee independence, and about how the partnership interacts with the board. A combined chair/CEO and the lack of a lead independent director were also of concern. The company's varied business segments for online and offline retail, consumer and digital, pose a range of ESG risks and opportunities that require more detailed reporting and shareholder engagement.

Governance concerns

We first raised our concerns about the lack of shareholder communication in 2015. Subsequently, we also expressed concern about insufficient board and committee independence.

Ahead of the 2018 annual shareholder meeting, we issued a public statement, calling for clarity on the company's board governance structure including the VIE structure, improved board independence (of at least 50%), the appointment of a lead independent director, and independent chairs for the nomination and governance committee and the compensation committee. In 2020 we went further and recommended voting against the election of the CFO to the board, in order to support more independent directors.

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In a call with the company in June 2021, we highlighted Alibaba's opportunity to improve its board independence by replacing a non-independent non-executive director with an independent director, who would ideally be female. The investor relations director said this was a useful suggestion and it would be relayed to the board.

ESG strategy and reporting

In 2017 we had asked for improved ESG strategy and reporting, sharing best practice examples. Therefore, we welcomed the publication of Alibaba's first ESG report in 2019, which focused on seven priorities. We provided feedback on this reporting, proposing improvements including more information on ESG governance, aligning with the UN Sustainable Development Goals, further disclosure on cybersecurity, carbon emissions, the inclusion of science-based targets and reporting based on the Task Force on Climate-related Financial Disclosures (TCFD). We also requested the inclusion of more strategic social aspects such as a human capital management strategy and metrics to align with the company's core values.

We also requested the inclusion of more strategic social aspects such as a human capital management strategy and metrics to align with the company's core values.

During a meeting at the company's Hong Kong offices in 2019, we responded to questions about our feedback on governance and structuring the team, which demonstrated that the company was thinking carefully about further improvements. We also urged the company to report annually, rather than every other year, as planned.

Outcomes

At the 2021 shareholder meeting, Alibaba did not propose the re-election of one of the non-independent non-executive directors, as we had suggested, meeting the goal of 50% board independence. In 2022, the company appointed an independent chair to the nomination and governance committee.

> **As part of establishing a credible plan to improve minority shareholder engagement, the company appointed a director responsible for engaging with shareholders on all aspects of ESG, leading to significantly improved shareholder engagement.**

The 2019 and 2020 reports provided more information on the VIE structures. This included information about the governance and the holding structures as well as the names of the individuals from the Alibaba Partnership who form the limited liability companies as part of the VIE structure.

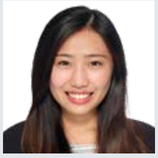
As part of establishing a credible plan to improve minority shareholder engagement, the company appointed a director responsible for engaging with shareholders on all aspects of ESG, leading to significantly improved shareholder engagement.

> **Alibaba has made significant progress, and we have an established and ongoing dialogue with the company.**

At the end of 2021, we were pleased to receive more information about the company's ESG strategy, and confirmation that it would issue a 2022 ESG report and then report annually. It also announced a new sustainability development committee reporting into the board.

Next steps

Alibaba has made significant progress, and we now have an established and ongoing dialogue with the company. It has assured us that its upcoming ESG report will include enhanced disclosure on key topics. We will continue to engage on the separation of the chair and CEO roles, the appointment of a lead independent director and improved board director engagement with minority shareholders.



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Strategy, risk and communication

Regional public policy highlights

Throughout 2022 we have participated in public consultations and meetings with government officials, financial regulators, stock exchanges, industry associations, and other key parties to contribute to the development of policy and best practice. The aim is to protect and enhance value for our clients by improving shareholder rights. This is a selection of some of the key market trends and highlights.

Brazil

Investors in Brazil are increasingly using voting as a tool for stewardship. In 2022 we saw several shareholder candidates proposed for board elections, in response to a lack of independence and diversity.

Interference by the Brazilian government, the controlling shareholder of Petrobras, resulted in two board elections in four months at the oil company. We opposed the proposed slate due to the deterioration in independence and diversity. We used the cumulative voting system to recommend support for the election of an independent director at Klabin, in addition to the independent director elected at the 2021 annual shareholder meeting under the separate election system.

The legislation allowing candidates to be nominated by minority shareholders has been in place for a long time but was rarely used. It is a positive sign that domestic, as well as international, investors are prepared to act because they see the value of diverse and independent boards.

The lack of a structured process for board succession and the action taken by minority shareholders to nominate candidates in parallel with the controlling shareholder nomination does not always lead to good outcomes in terms of independence and diversity of skills. However, the market is going through a learning curve, and we expect stewardship to lead to better boards.

In another encouraging sign, feedback that we had provided to the Association of Capital Markets Investors (AMEC) was reflected in the market priorities for the coming year. The Comissão de Valores Mobiliários will prioritise the improvement of the annual shareholder meeting voting system and the disclosure of executive remuneration.

Continental Europe

We submitted a response to a consultation by the European Financial Reporting Advisory Group on the EU Sustainability Reporting Standards. Our response focused on the need for the standards to include transparency on the lobbying activities of companies, particularly indirect lobbying conducted by industry associations.

We co-signed a letter co-ordinated by Farm Animal Investment Risk and Return (FAIRR) to the Food and Agricultural Organization of the United Nations (FAO), calling on the FAO to produce a global roadmap towards a sustainable global food system by 2050. In the letter, we underlined that it is crucial that the roadmap aligns with the Paris Agreement's goal of limiting global warming to 1.5°C while ensuring the protection and restoration of nature and achieving food and nutrition security goals.

It is a positive sign that domestic, as well as international, investors are prepared to act because they see the value of diverse and independent boards.

Japan

As a member of the Asian Corporate Governance Association (ACGA), we attended a virtual delegation meeting in Japan with Japan's Financial Services Agency (FSA), the Japan Exchange Group (JPX), the Ministry of Economy, Trade and Industry (METI) and the Japanese Institute of Certified Public Accountants. We outlined our policy expectations for shareholder rights and corporate governance best practice.

We also responded to the PRI's request for input on its draft response to the FSA's consultation on ESG evaluation and data providers. In the consultation response, we provided our requirements for clear and detailed disclosures. We want to see companies implement public reporting that is mandatory for supporters of the Code of Conduct for ESG Evaluation and Data Providers, and to explain in detail which principles and concepts they comply with and how.

Taiwan

We wrote to Taiwan's Financial Supervisory Commission to endorse comments from the Asian Corporate Governance Association on the draft amendments of regulations governing the acquisition and disposal of assets by public companies regarding related party transactions (RPTs). These are an important issue, particularly for minority shareholders, and require significant consideration.

We explained in our letter that we expect RPTs, especially finance-related transactions, to include detailed disclosure on the rationale of the use of a connected party, the terms of agreement, and the audit and assurance mechanisms put in place to ensure that the transactions are conducted in a fair and transparent manner over the agreement period, not only during the initial phase.

UK

As a member of the CDP's Technical Working Group, we responded to a public consultation survey on CDP water-related indicators for financial institutions. CDP, with input from investors and their representatives, is developing the first set of standardised, global water security reporting indicators for the financial sector. We previewed the list of new water indicators and shared feedback confidentially with CDP. The water-related indicators included in the consultation represent the second phase of indicator development, which are quantitatively focused. An initial set of water security indicators have already been incorporated into a nature-related module as part of CDP's 2022 climate change questionnaire for the financial sector.

We responded to an Institutional Investors Group on Climate Change (IIGCC) consultation about how investors and companies should approach offsetting, both as EOS at Federated Hermes and Federated Hermes Limited. We welcomed the principles as an important step towards holding investors and portfolio companies to account for delivering credible net-zero strategies, but emphasised some areas that could be clarified. We suggested doing more to explain that emissions reduction for investors and their portfolio companies is an absolute priority and should be the primary focus, considering the significant emission cuts that need to happen up to 2030.

We spoke at a roundtable at Westminster, organised by ShareAction and the UK Sustainable Investment and Finance Association. It was attended by cross-party representatives from the House of Commons and the House of Lords. Other attendees came from the financial sector and civil society. The goal was to raise the ambition of UK policymakers and action by the finance sector ahead of the Convention on Biological Diversity COP15.

We highlighted the importance of engagement and stewardship for investors to tackle biodiversity loss. We outlined the actions we had taken to advocate for an ambitious and transformative Global Biodiversity Framework, including formal participation in the negotiations on behalf of Finance for Biodiversity, position papers on aligning financial flows and an open letter to governments.

> **We suggested doing more to explain that emissions reduction for investors and their portfolio companies is an absolute priority, considering the significant cuts that need to happen up to 2030.**

We emphasised the need for voluntary action from the financial sector to be complemented by an enabling regulatory environment, with effective policies that encourage the protection and restoration of biodiversity and stimulate action by the financial sector.

US

We submitted a letter to the Securities and Exchange Commission (SEC) in response to the proposed climate disclosure rule. We welcomed the SEC's efforts to enhance reporting requirements for companies to include material ESG factors and consider disclosure rules on climate change, including the requirement to disclose Scopes 1 and 2 emissions, and material upstream and downstream Scope 3 emissions.

We are supportive of the rule given that it would lead to more timely, accurate, comprehensive, comparable, and standardised information disclosed by public and private companies. We are confident that this disclosure would contribute to informed capital allocation and business decisions, resulting in improved value creation and risk mitigation for investors.

We worked closely with the Environmental Defense Fund (EDF), a US-based non-profit environmental advocacy group, to produce a letter to send to the International Financial Reporting Standards (IFRS) Foundation. This laid out specific methane-related disclosure enhancements for oil and gas exploration and production, midstream operators, and electricity and gas utilities and distributors.

We responded to the IFRS Foundation-led consultation on two sustainability draft standards developed by the International Sustainability Standards Board (ISSB). Overall, we were supportive of the direction the ISSB general requirements and climate standards had taken and provided suggestions to enhance the standards. These included improved clarity on key terms, recognising important frameworks such as the Taskforce on Nature-related Financial Disclosures, plus other improvements.

We were a co-signatory of a letter on paid sick leave (PSL) co-ordinated by the Interfaith Center on Corporate Responsibility (ICCR), which was sent to over 40 companies and made the business case for a permanent PSL benefit for all workers in the US. The letter was signed by 150 institutional investors and their representatives that collectively represented US$3.6tn in assets.[1] While the companies came from a range of sectors, there was an emphasis on retail and restaurant companies where frontline workers are most exposed to the public and, by extension, potential illness.

[1] https://www.iccr.org/investors-escalate-pressure-companies-adopt-paid-sick-leave-policies

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Federated Hermes is a global leader in active, responsible investing.

Guided by our conviction that responsible investing is the best way to create long-term wealth, we provide specialised capabilities across equity, fixed income and private markets, multi-asset and liquidity management strategies, and world-leading stewardship.

Our goals are to help people invest and retire better, to help clients achieve better risk-adjusted returns, and to contribute to positive outcomes that benefit the wider world.

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Our investment and stewardship capabilities:

- **Active equities:** global and regional
- **Fixed income:** across regions, sectors and the yield curve
- **Liquidity:** solutions driven by four decades of experience
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- **Stewardship:** corporate engagement, proxy voting, policy advocacy

Why EOS?

EOS enables institutional shareholders around the world to meet their fiduciary responsibilities and become active owners of their assets. EOS is based on the premise that companies with informed and involved investors are more likely to achieve superior long-term performance than those without.

For more information, visit **www.hermes-investment.com** or connect with us on social media: