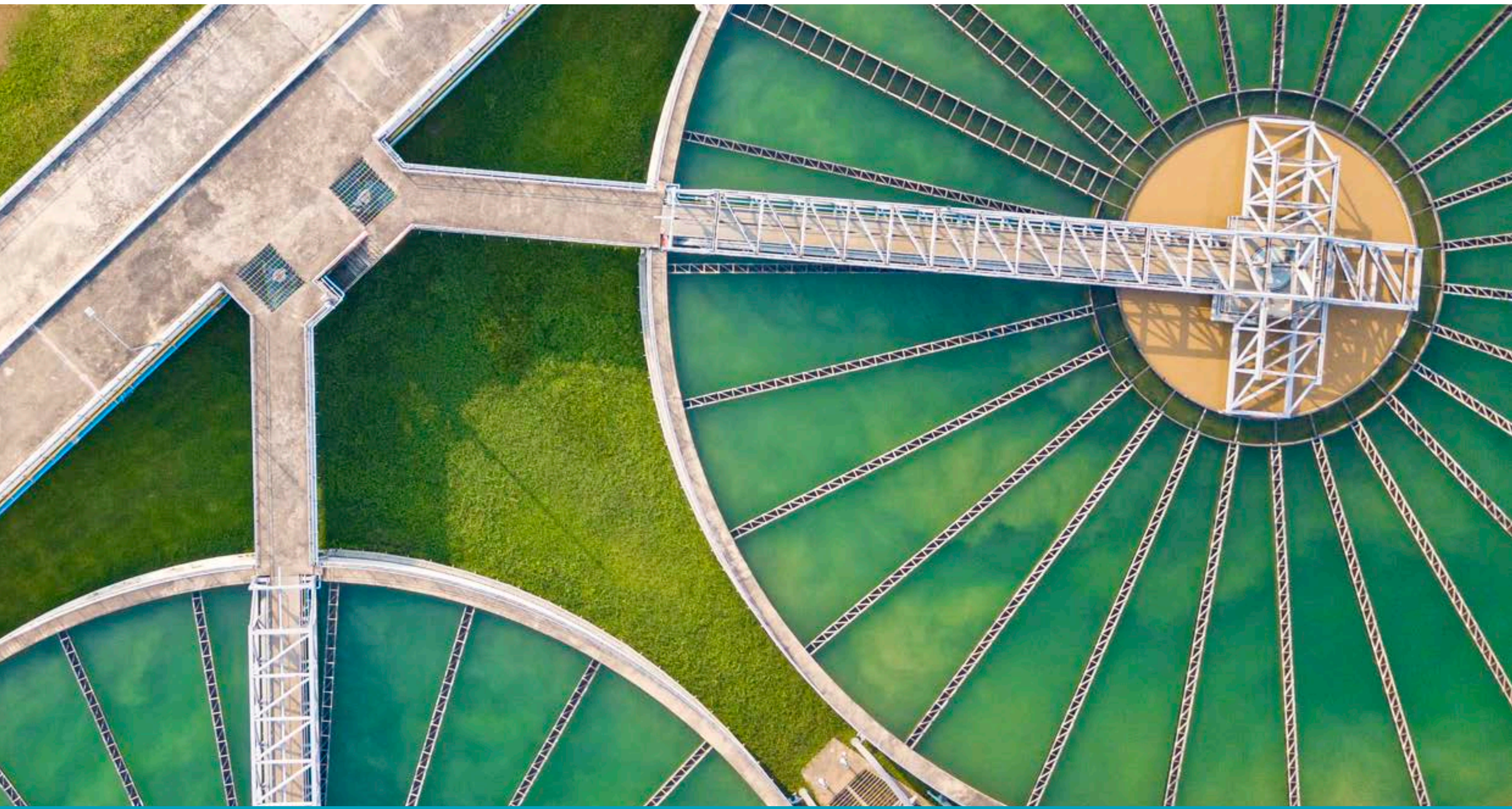
ROBECO
The Investment Engineers



ACTIVE OWNERSHIP REPORT

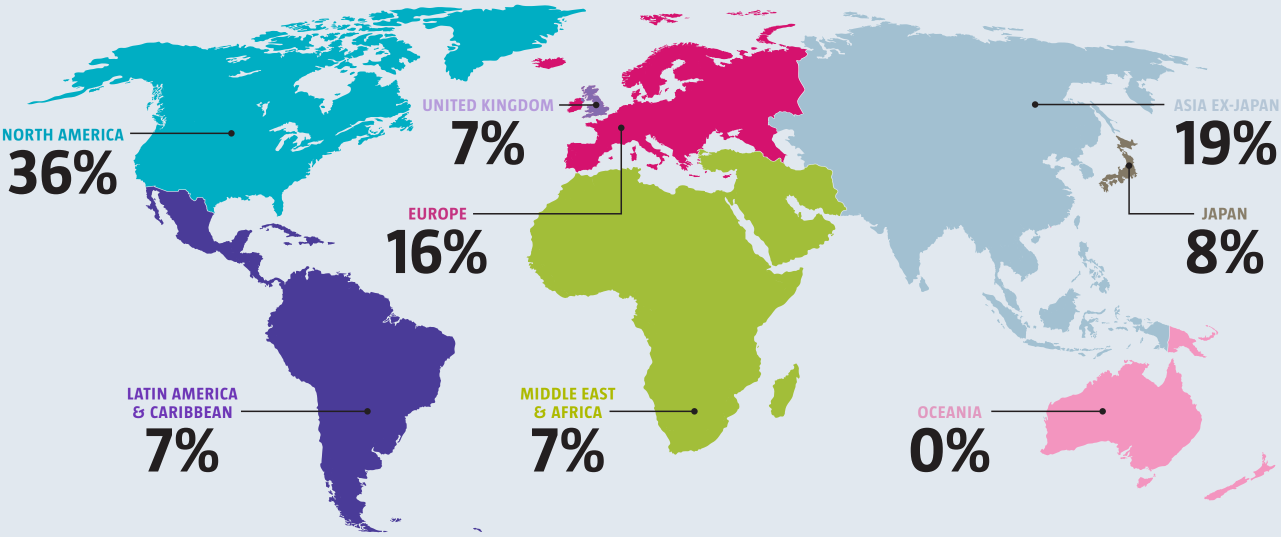
ROBECO | 01.07.2022 - 30.09.2022

Q3 2022

Sustainable Investing Expertise by ROBECOSAM

Q3|22 FIGURES ENGAGEMENT

Engagement activities by region



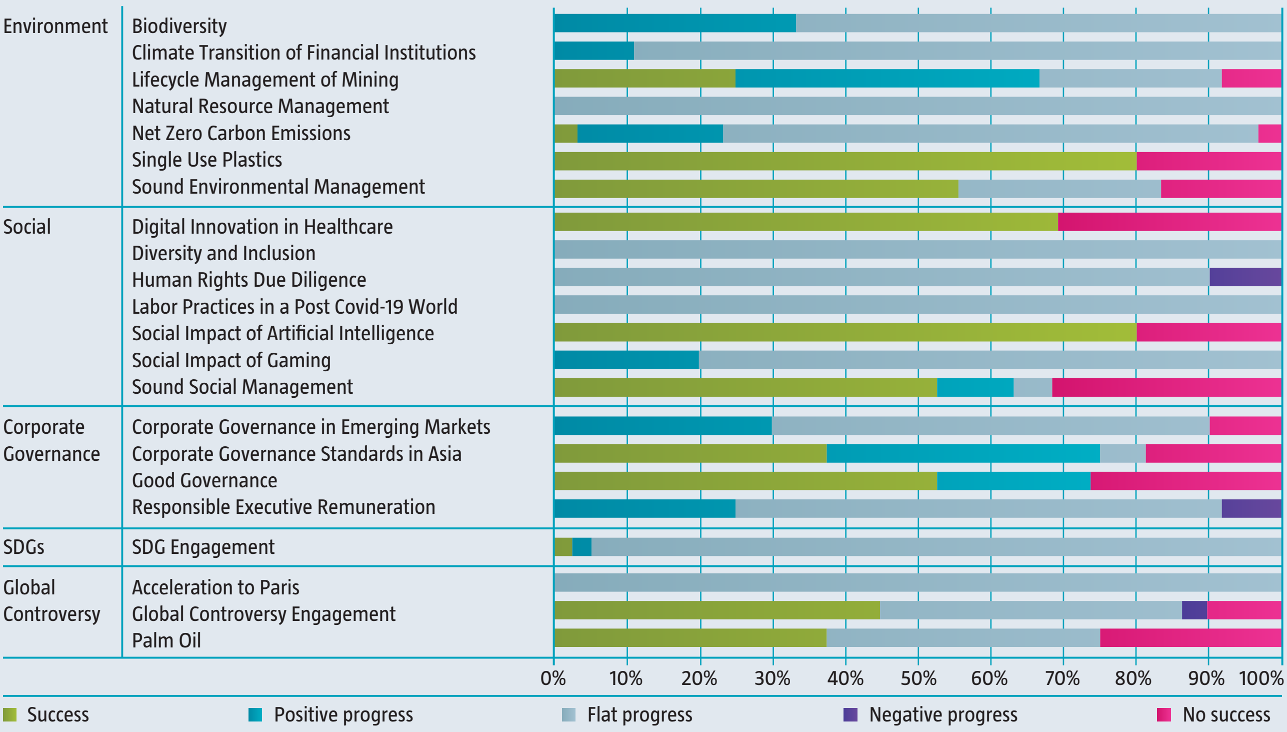
Number of engagement cases by topic*

	Q1	Q2	Q3	Q4
Environment	48	55	40	
Social	20	26	21	
Corporate Governance	20	23	14	
SDGs	15	30	18	
Global Controversy	25	19	14	
Total	128	153	107	

Number of engagement activities per contact type

	Q1	Q2	Q3	Q4	YTD
Meeting	1	1	5		7
Conference call	81	91	59		231
Written correspondence	89	125	78		292
Shareholder resolution	0	1	0		1
Analysis	16	27	22		65
Other	1	11	1		13
Total	188	256	165		609

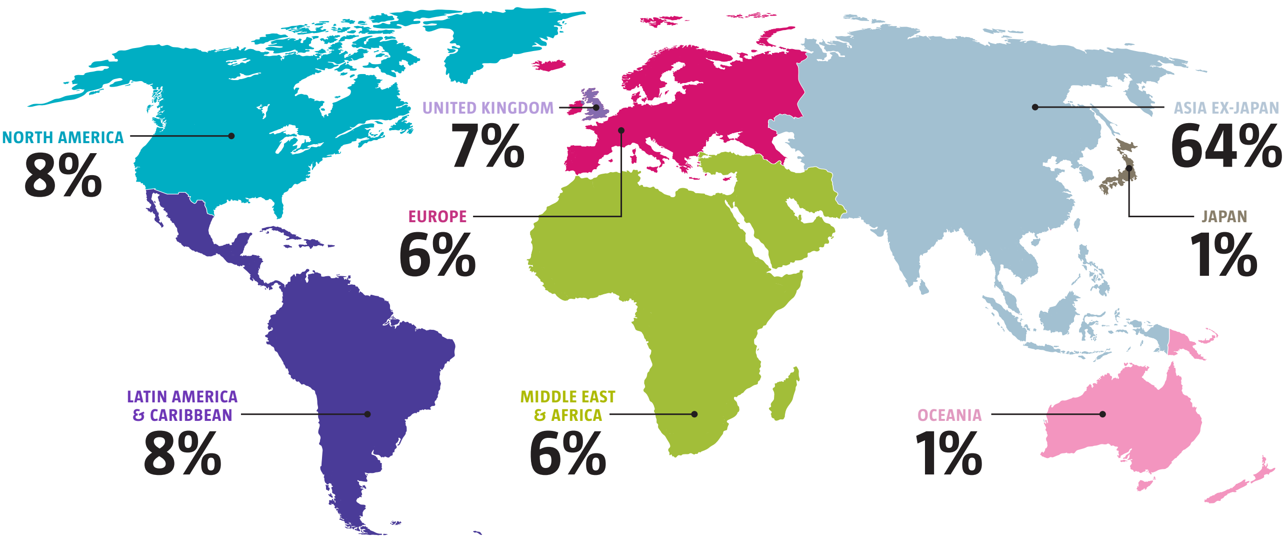
Progress per theme



* Due to a change in Robeco's methodology to account for engagement cases, numbers are expected to differ from previous quarters.

Q3|22 FIGURES VOTING

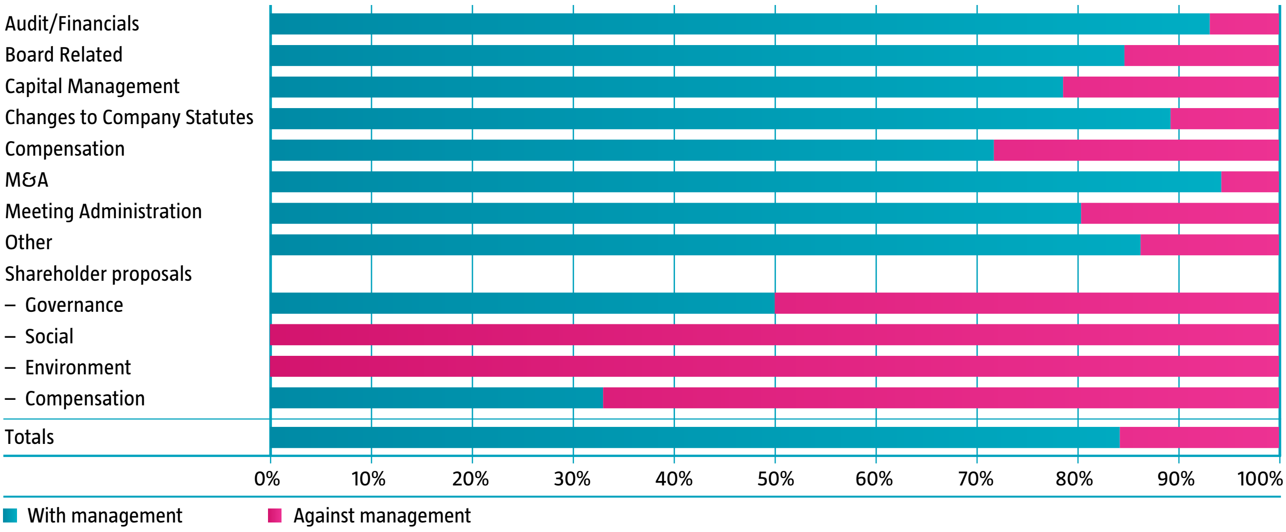
Shareholder meetings voted by region



Voting overview

	Q1	Q2	Q3	Q4	YTD
Total number of meetings voted	1,076	4,308	1,053		6,437
Total number of agenda items voted	9,268	53,407	8,082		70,757
% Meetings with at least one vote against management	56%	60%	48%		58%

Votes cast per proposal category



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INTRODUCTION

During the third quarter of 2022, Robeco has been actively pushing the frontiers of sustainable investment by sharing our intellectual property with our clients, while continuing to work with our investee companies on the engagement areas we deem most critical.

The new quarter was marked by a great step forward for Robeco and its clients as we launched our Sustainable Investing (SI) Open Access Initiative. Through this initiative, we are sharing some of our most valuable proprietary data with our clients and academics, including Robeco's proprietary Sustainable Development Goal (SDG) scores and methodology, in the hope that we can work together to build a more robust sustainable investment landscape.

Meanwhile, on the engagement side, we have launched two new engagement themes. Our new Diversity and Inclusion engagement program is working to address the societal inequalities mirrored throughout gender and ethnic pay gaps, discriminatory company policies and unequal promotional opportunities. By considering their most vulnerable employees at each step of their human capital management, companies can strengthen employee attraction, lower turnover costs and benefit from diverse perspectives and skillsets. Through this theme, we hope to help companies elevate each part of their workforce, and thus create value for both them and society.

On the environmental side, in line with the rising summer temperatures and climate change-induced droughts across the world, we have initiated a new engagement stream on Natural Resource Management. This focuses on companies working in water and/or waste-intensive sectors and will look not only at strengthening companies' water and waste policies, but also whether they have strong operational processes around emergency situations. The engagement theme will also address chemical waste and seabed mining and tailings.

Elsewhere in this report, we provide an update on some of our ongoing engagements. With the quarter marking the mid-point of our three-year engagement around the Climate Transition of Financial Institutions, we see that only few banks are on credible net-zero trajectories. Many still lack adequate targets and essential carbon emissions data throughout their loan books. These are all issues that were echoed by the shareholder proposals we supported at numerous banks during the 2022 proxy voting season.

The aftermath of the proxy season always provides grounds for engagement on the topic of Responsible Executive Remuneration, as companies are trying to understand investors' reasons for voting against pay-related agenda items. During our update, we delve into some of the best practices we advocate for when it comes to executive remuneration, as well as some concerning trends we see across companies. These include the growing use of ill-designed sustainability-linked performance pay packages which are being used as a remuneration cushion, rewarding executives during times of bad company performance.

We enter the new quarter with clearly laid out engagement priorities and a strong mandate for transparency and look forward to the change to come.

Carola van Lamoen
Head of Sustainable Investing

Focus on companies' impacts on human and natural resource management

DIVERSITY AND INCLUSION & NATURAL RESOURCE MANAGEMENT

LAURA BOSCH – *Engagement specialist*
ANTONIS MANTSOKIS – *Engagement specialist*
SYLVIA VAN WAVEREN – *Engagement specialist*

More and more investors are moving beyond measuring sustainability only through the material environmental, social and governance (ESG) risks companies are facing, and increasingly try to identify the impacts that companies' activities have on society, whether through their products or processes. In this interview, Laura Bosch, Antonis Mantsokis and Sylvia van Waveren share how Robeco's new Diversity and Inclusion, and Natural Resource Management themes aim to explicitly address some of the key adverse environmental and social impacts companies can have.

Why are we launching these engagement themes, and where do they differ from other programs?

The focus of sustainable investing is increasingly shifting from the idea of single financial materiality to the concept of double materiality, whereby the focus is no longer only on how sustainable development impacts companies but also how companies contribute to this development. This includes both positive and adverse impacts, where addressing adverse impact has been the key driver behind our new engagement themes. Adverse impact as a concept ranges from water emissions and negative biodiversity impacts to social violations and gender pay gaps. Impacts which the European Commission is now making investors report on, in particular through the Principal Adverse Impact Indicators (PAI) defined in the EU Sustainable Finance Disclosure Regulation (SFDR). The regulation requires investors in the EU to disclose performance against at least the mandatory PAIs for their holdings, using a set of ESG metrics reflecting their negative externalities.

While we have been addressing adverse impacts within our engagement program for many years, we took the opportunity to identify potential gaps in our engagement approach using the mandatory list of PAIs in 2021. As a result of the analysis, we are now launching two new engagement themes explicitly covering Diversity and Inclusion and Natural Resource Management. The two themes aim to support companies in facing some of their core negative impacts around their human and natural resource management, and push for more transparency as required by the PAIs.

These engagement programs differ from our conventional themes as they were designed to incorporate a higher degree of flexibility. They need to gradually increase coverage, as they follow the development of PAI-related data and increasing engagement demand. The two themes are expected to run continuously, instead of over the usual three years. Moreover, timelines for the engagement dialogues can be shortened if successful outcomes are achieved at an earlier stage.

DIVERSITY AND INCLUSION

sitting down with Laura Bosch and Antonis Mantsokis

Firstly, looking at Diversity and Inclusion – why is this relevant for investors?

The relevance of Diversity and Inclusion (D&I) for investors can be understood through the double materiality lens. From a financial standpoint, D&I can enhance corporate performance in many ways: recruiting and retaining the best talent, having stronger customer orientation, enhancing corporate reputation, and improving decision-making and innovation outcomes. Many industries are becoming increasingly knowledge-intensive, which is materialized financially by the more prominent role that intangibles play in global balance sheets.

Therefore, human capital management strategies, including the promotion of diversity and inclusion, are significantly important in determining a company's underlying quality and intrinsic value. Investors should therefore integrate such factors into their investment approach to formulate better-informed decisions.

At the same time, the benefits stemming from an inclusive and diverse workforce flow through to the macro environment and have a societal impact. Barriers for women and minorities to enter the labor market, such as pay distortions, social and cultural factors, and outright discrimination, work against achieving parity and have a financial cost. Poor allocation of human resources that wastes an individual's education, talent and potential, contributes to this cost. The resultant welfare gains after removing the obstacles are estimated to be more significant. Providing employment opportunities and equal remuneration to minority groups can minimize structural wealth gaps between societal groups. Subsequently, this would have a direct impact on society and the economy as a whole.

What are the aims of the theme?

We formulated five engagement objectives to facilitate our dialogue on D&I. The first step towards creating a more diverse workforce is developing a D&I policy, resulting in a higher-level commitment and a consistent approach to advance D&I throughout the company. It should include a set of time-bound goals that are sufficiently ambitious to effectively diversify a company's workforce. Once these goals are in place, a critical next step is to clearly define how to establish D&I as a priority among corporate leaders and hold them accountable for their contributions. This includes having a sufficiently diverse leadership and board of directors, latter of which is measured by the PAIs.

Our second objective focuses on how companies define their D&I implementation strategies and measures of success for aligning their talent management strategy with their business goals and D&I objectives over the different stages of the employee lifecycle. Thirdly, we encourage companies to disclose workforce diversity data, focusing not only on ethnic or gender diversity across different employment bands and employee levels, but also incorporating other diversity components.

The fourth objective focuses on overall pay equality. Companies should undertake audits to ensure they address any pay gaps in their D&I strategy. We expect companies to provide quantitative statistics, complemented by qualitative assurances, for both adjusted and unadjusted median pay gaps, as required by the mandatory PAIs. Finally, we encourage companies to promote an inclusive culture by taking a strategic approach to shaping attitudes and behaviors in the workplace that can shift workplace culture in a meaningful way.

How do you decide which companies should be under engagement?

The lack of data is the main challenge identified by investors when assessing companies' efforts on diversity and inclusion. With that in mind, we first identified those industries where disclosure of diversity data is lagging. We looked at the PAI indicators using data produced by MSCI and the S&P Global Corporate Sustainability Assessment (CSA). For our engagement, we prioritized the 20 industries with the lowest levels of disclosures.

Within those selected industries, we identified the first set of companies by screening those that fail to disclose their unadjusted gender pay gap, in line with PAI requirements, and also did not answer the diversity-related questions in the CSA questionnaire. The questionnaire

> **'ONCE (D&I) GOALS ARE IN PLACE, A CRITICAL NEXT STEP IS TO CLEARLY DEFINE HOW TO ESTABLISH D&I AS A PRIORITY AMONG CORPORATE LEADERS AND HOLD THEM ACCOUNTABLE FOR THEIR CONTRIBUTIONS.'**
>
> LAURA BOSCH I ANTONIS MANTSOKIS

looks at aspects like age, disabilities, sexual orientation and broader human capital-related factors. We also considered gender-focused data sources, namely RobecoSAM's gender score and the Equileap score, which assess the inclusion of women across companies. Additionally, we collaborated closely with our portfolio managers and analysts to decide upon the final selection of companies.

What other actions will be taken in line with this engagement?

The Black Lives Matter and MeToo movements both highlighted the negative impact of today's systematic inequalities. Investors have increasingly been putting pressure on companies by supporting social-related shareholder resolutions, and stakeholders are holding those companies that do not promote D&I to account.

In line with this engagement, we will continue to vote against management on specific agenda items when the company fails to incorporate minimum standards on gender diversity at the board level. We will continue to evaluate issues on a case-by-case basis, and support those shareholder resolutions that aim to resolve social issues such as racial equality. Additionally, we will explore filling shareholder resolutions focusing on promoting D&I in those companies where we see no progress and the social issues continuously persist.

What challenges do you expect to face and what are the outcomes you expect to achieve?

Promoting D&I is a challenging topic at its core due to differences in company cultures and regional practices. There are many benefits stemming from promoting diversity metrics or goals, and having D&I policies in place. However, practically improving inclusion is not always addressed with equal importance, and it is much more challenging to measure it. In many cases, it isn't easy to assess if the spirit of the policies in place is accomplished in practice.

Another significant hurdle that we expect to face is how to equally address all aspects of diversity, and move the conversation beyond simply looking at gender. There are still many countries where identifying as LGBTQ+ remains illegal, and cultural norms prohibit companies from promoting an inclusive culture. Moreover, processing employees' D&I-related data is prohibited in many countries, due to privacy restrictions (i.e., GDPR in the EU), making it difficult to have targeted policies. In addition, companies usually focus on promoting female representation on the board or at the top management levels, and stick to a mechanical implementation of gender-only quotas. Promoting practices that address the benefits of the integration of various minority groups will be challenging.

Lastly, pay equality is an issue not easy to resolve. According to World Economic Forum's Global Gender Gap report 2020, it will take 257 years to achieve equal pay for women and men at work at the current rate. Pay disparity, though primarily gender-focused, also exists regarding race, ethnicity, sexual orientation, disabilities and age. Thus, it is challenging to promote structural solutions in pay equality when in many countries there are no regulatory requirements to tackle the broader aspects of the pay gap.

ENGAGING ON NATURAL RESOURCE MANAGEMENT

by Sylvia van Waveren

Moving to the environmental front - Why is Natural Resource Management relevant for investors?

The world is facing a dire shortage of freshwater, a situation that is set to only get worse due to urbanization, population growth, climate change and socio-economic development. The World Research Institute's Aqueduct Water Risk Atlas reveals that 44 countries currently face high baseline water stress covering one-third of the world's population.

Companies operating in highly water-stressed regions are not only exposed to these risks but also often enhance them through their own water usage and pollution. Disregarding both their impacts and risks can impact corporate valuations through higher operating costs, thus threatening their viability if they do not sustainably manage their water use. This risk is estimated to amount to USD 301 billion for companies, while the cost of addressing their adverse impacts is estimated to be less than one-fifth of that, at USD 55 billion.

It is therefore important for investors to engage with such companies on having resilient water management strategies. Those with poor strategies are more likely to experience production disruptions, stranded assets and community conflicts, all resulting in higher comparative operational and fixed costs which will reduce their overall rate of return.

What are the aims of the theme?

To act upon these risks, Robeco has expanded its environmental engagement program to include the responsible management of natural resources and the mitigation of adverse impacts on the environment. The engagement theme aims to address the impacts of corporate operations related to their intensive water use and generation of waste.

Our engagement strives to minimize risks through a set of objectives that aim to enhance corporate disclosures on their management of water and waste issues. The engagement will also address major issues such as seabed mining and tailings, and the gross emissions of PFAS chemicals into waterways.

How will you assess which companies should be under engagement?

Companies need to account for the amount of freshwater that is needed to make certain products – often drawn from places where water is already scarce. The discharge of wastewater also remains problematic and therefore needs to be addressed. To address these issues, we focus on companies for which the management of water and waste generation and disposal management is a financially material issue, or where corporate operations have a significant actual or potential negative environmental impact due to water or waste issues.

Thus, in our water engagements, the focus is on companies operating in high water-stress areas as well as those deemed to have high water consumption. In the waste engagements, the focus is on companies that generate hazardous waste such as PFAS chemicals and (threaten to) pollute the environment, including companies exploring seabed mining and tailings.

In July 2022, we started engaging with the first group of six companies. They were chosen using a bottom-up and fundamental approach by Robeco's research and investment analysts. They belong to three sectors: Chemicals (fertilizers and mines); Oil and Gas (shale gas); and Paper and Pulp (operating in South Africa, a water scarce area).

What other actions will be taken in line with this engagement?

We have developed a water and waste management framework tool to assess how well a company has incorporated the management of such risks into their practices. This framework, depicted in Figure 1, evaluates several indicators related to their water and waste policies, their risk management programs, their metrics, targets and disclosures, among others. The insights from this assessment inform our engagement priorities and facilitates the tracking of progress against our engagement objectives.

Figure 1 | Water and waste management evaluation framework

Level 0 Unaware	Level 1 Aware	Level 2 Capacity Building	Level 3 Operational Integration	Level 4 Strategic Risk Assessment
Companies are neither aware nor acknowledge water/ waste management risks.	The company acknowledges that water stress and/or waste generation present business risks. The company adopts a water and waste management policy including initial water and waste risk reporting.	The company develops and evaluates its water and waste policies, its management systems and processes, and starts to report on practice and performance.	The company improves its operational practices, assigns senior management or board responsibility for water or waste management and provides comprehensive disclosures on its water use or waste management practices and performance.	The company develops a more strategic and holistic understanding of the risks and opportunities related to the high water use and waste generation and integrates this into its business strategy, its remuneration policies and its capital expenditure decisions.

Another important action is recording incidents and controversies that had adverse environmental impacts, such as water depletion and pollution. Frequent involvement in these types of incidents is a sign of exposure to ESG risks and a company's failure to manage them. Incidents that go unmanaged can potentially lead to an erosion of shareholder value. We base our work on UN Global Compact and OECD guidelines.

What have been your first insights and how will you continue?

We expect that our methodology to identify companies to engage with will continue to evolve and be refined as the relevant data continues to improve and become more broadly available, including that used to measure the SFDR PAIs. We believe that engagement is one of the tools that we can use in addressing and mitigating adverse impacts at the company level and were pleased with companies' initial openness to discuss their approach to natural resource management. ■

Financing the climate transition

CLIMATE TRANSITION OF FINANCIAL INSTITUTIONS

ROBERT DYKSTRA – *Engagement specialist*

It has become increasingly clear that the banking sector has a critical role to play in the low-carbon transition. Banks can facilitate investments in low-carbon solutions and encourage emission reductions through climate-aware financing and engagement with their clients. Banks that continue to finance activities not aligned with the low-carbon transition create significant transition and physical risks associated with accelerating global warming.

The fast-evolving landscape

Various stakeholders including investors, governments and the public have put an increasing amount of pressure on the financial sector to advance the economy-wide transition towards net zero emissions. This was highlighted at COP 26 in November 2021, which saw several guidelines emerge to help financial institutions measure their 'financed emissions' – those associated with loans, investments and other financial products. These guidelines include the Partnership for Carbon Accounting Financials (PCAF), the Paris Agreement Capital Transition Assessment (PACTA) and the Science Based Targets Initiative's (SBTi) guidance for the financial sector. Several other initiatives have also been started to help the financial sector align with net zero, such as the Glasgow Financial Alliance for Net Zero (GFANZ) and the Net Zero Banking Alliance (NZBA).[1]

While many banks are dealing with operational challenges such as emission data collection and new governance structures, the expectations around disclosures and targets are becoming ever-more stringent. For example, the NZBA has outlined a timeline for setting sector-specific decarbonization targets by 2024. However, these targets should also be aligned with a credible net zero emission scenario, such as the ones established by the International Energy Agency (IEA). Several banks have already set targets that now need to be readjusted to be aligned with a particular scenario. Many banks are also expected to disclose fossil fuel lending policies that outline the criteria for denying clients access to loans or capital markets.

A collaborative engagement approach

With our three-year engagement program on the climate transition of financials having reached its mid-point, we take stock of the progress made and upcoming challenges that banks will face in executing their climate strategies. At the start of this engagement theme, we selected 10 banks amongst our and our clients' portfolios with significant exposure to carbon-intensive assets.

To maximize the effectiveness of our engagement strategy, we collaborate with the Institutional Investor Group on Climate Change (IIGCC), which coordinates a larger investor initiative on banks' climate strategies. The IIGCC, in partnership with the Transition Pathway Initiative (TPI), is developing a framework to assess how prepared banks are for the low-carbon transition. The framework consists of many indicators that have been selected following significant investor consultation and tested on 27 banks from across the globe based on disclosures published up to February 2022. Over the coming months, the IIGCC and TPI will continue their consultation on these indicators to improve and fine-tune the framework so that a final version can be published in late 2022.

'BANKS SHOULD EXPAND THEIR NET ZERO COMMITMENTS TO INCLUDE ALL HIGH-RISK SECTORS IN ALL MATERIAL BUSINESS SEGMENTS. THIS MEANS NOT ONLY FOCUSING ON REDUCING FINANCED EMISSIONS THROUGHOUT THEIR LOAN BOOKS, BUT ALSO IN CAPITAL MARKET ACTIVITIES SUCH AS UNDERWRITING AND M&A.'

ROBERT DYKSTRA

The indicators are grouped into the following six areas and provide a comprehensive picture of a bank's net zero transition plan:

1. Net zero commitments
2. Short and medium-term targets
3. Decarbonization strategies
4. Climate governance
5. Climate policy engagement
6. Audit and accounts.

Based on the first round of assessments conducted earlier in 2022, average alignment with credible net zero trajectories amongst banks is relatively low. This is in part due to the lack of disclosure of carbon emission data throughout their loan books, but also because of insufficient target-setting at the time of the assessment. These six elements of the framework correspond with our existing engagement objectives, which are based on the four pillars of the Task Force for Climate-related Financial Disclosure (TCFD).

Future steps and upcoming challenges

The assessment outlines several areas for banks to improve their climate strategy, primarily through enhanced disclosures and financed emission reduction targets. Specifically, banks should expand their net zero commitments to include all high-risk sectors in all material business segments. This means not only focusing on reducing financed emissions throughout their loan books, but also in capital market activities such as underwriting and M&A.

1. An overview of Robeco's sustainable investing memberships, statements & principles can be found here: www.robeco.com/docm/docu-relevant-codes-and-memberships.pdf

More transparency on how banks engage with clients is also expected in the coming years. For instance, banks should disclose explicit financing conditions for clients whose transition plans are not aligned with a net zero emissions pathway. These conditions could be outlined in a dedicated coal or oil and gas lending policy which we have seen at several major banks. This includes aligning all high-risk sector policies with a 1.5°C warming scenario. For example, the IEA's Net Zero Emissions by 2050 scenario requires banks' coal sector policies to include:

- No financing of additional capacity for thermal coal operations.
- Phasing out of financial services and portfolio exposure to unabated coal-fired power generation by 2030 in the EU and OECD countries, and in the rest of the world by 2040 at the latest.

These expectations have been echoed by shareholder proposals filed at numerous banks during the 2022 proxy voting season. Banks were asked to define their commitment to being net zero by 2050 and include a timeline by which they would stop all lending related to new fossil fuel supplies. Many banks found these requests overly prescriptive, as they did not take into account regional discrepancies in energy demand, such as heavier coal dependency in emerging markets. Nonetheless, large groups of shareholders, including Robeco, supported these proposals with the aim of making banks' net zero commitments more credible.

In the upcoming second half of the engagement theme, we will use the outcomes of this assessment framework to emphasize the changes that we expect banks to make. So far, several banks are making significant progress, while others appear to be lagging. This is in part due to the varied pressure banks anticipate from looming sustainability regulations in the EU and North America.

Overall, the governance around climate-related financing has been one of our engagement objectives that has seen the most progress. Unfortunately, our objectives around risk management and strategy have seen the least progress. Therefore, we will push for improvements in sector decarbonization strategies and scenario analyses in our upcoming dialogues.

CASE STUDY

Our engagement with Sumitomo Mitsui Financial Group (SMFG) is conducted through three different channels: directly with the company; collaboratively through the Asia Research and Engagement (ARE) group; and as members of the IIGCC. Over time, we have seen an increase in the bank's receptiveness to investor feedback. As an example, SMFG was previously a laggard in the disclosure and transparency of its climate-related financing. However, once the company recognized that investors had short-term expectations related to net zero commitments, the bank began to act. SMFG reorganized its internal governance structure to allocate more resources to climate risk management and data collection throughout its business segments. These changes have in turn led to a significant increase in the quality of available disclosures.

The pay for performance crisis

RESPONSIBLE EXECUTIVE REMUNERATION

MICHIEL VAN ESCH – *Engagement specialist*

Executive remuneration often is one of the touchiest topics between investors and company managements. Firstly, there is the discomfort of a group of outsiders forming an opinion on how (and how much) someone should get paid. Secondly, there are often discrepancies between how well management think they have performed and whether investors agree that this actually has created value for them. Yet, the topic of executive remuneration has been relevant since the foundation of the first public stock company and remains a key governance instrument today.

In 2019, the EU's amended shareholder rights directive SRD 2 was passed into national legislation across the continent, giving shareholders the right to a vote on remuneration on a structural basis. Similar as in the US, shareholders have an advisory vote on the remuneration report. But they also get a formal say on the review of the remuneration policy at least every four years.

In the second half of 2020, Robeco conducted research into best practices for executive remuneration. An engagement project was initiated in order to make use of the new opportunities that the shareholder rights directive offers. For a set of European and US companies we have focused our engagement practices to improve corporate pay practices on four focus areas. These are (1) to better align pay with performance (including performance on sustainability); (2) to promote equity holding requirements (rather than option structures or cash pay-outs) to have a more straightforward alignment with shareholders; (3) to use ratios and benchmarks in order to avoid excessive pay discrepancies between and within organizations; and (4) to have strong and independent oversight from the supervisory board and feedback mechanisms towards its shareholders.

Taking stock of SRD 2

After a year and a half of engagement, it is safe to say that SRD 2 has had an impact. Almost directly after its implementation, we saw several remuneration practices being voted down, and requests for feedback calls picking up. Additionally, many companies are starting to look into incorporating non-financial measures (often ESG metrics) into remuneration packages. This is starting to become common practice across Europe, but is also a trend in the US. We also have seen companies align their reporting practices on remuneration with SRD 2. But have remuneration practices really become any better?

'WE CONTINUE TO SEE COMPANIES THAT HAVE POORLY DESIGNED STOCK PLANS WHICH FAIL TO INCENTIVIZE EXECUTIVES TO FOCUS ON DELIVERING LONG-TERM, SUSTAINABLE PERFORMANCE.'

MICHIEL VAN ESCH

Pay for performance, sustainability and the Covid-19 effect

At the start of our engagement, many companies had most of their financial performance metrics already in place. Even though for many of them we would we prefer that companies evaluate on risk and return-based metrics (such as the return on invested capital) rather than pure profit measures, at least companies' performance indicators and targets are often clearly communicated.

However, during the pandemic many corporates decided to drop these targets as the world's economic circumstances were duly turned upside down. Some companies dropped annual bonuses altogether, but many continued to pay out their bonuses under the argument that the pandemic is an external circumstance that does not relate to company performance. This logic seemed dominant in conversations, particularly in the US. For those companies we focused our engagement on alignment with the shareholder experience. It is common for companies to attribute strong stock performance in economic booms to management and to blame external factors for poor performance during economic downturns.

The introduction of sustainability-related metrics often is a good thing and sometimes we encourage it. However, we have also noted that some companies use sustainability performance as a remuneration cushion. When financial performance was close to zero, sustainability metrics were all met, safeguarding executive pay-outs but without strong disclosure. During our conversations, we aimed to make sure that sustainability metrics are measurable, relevant to the strategy, and sufficiently ambitious.

One common aspect to look out for are targets around metrics on sustainable product portfolios. Many companies set targets to improve the percentage of sustainable revenues that could be attributed to their product pipelines. This could be a valid measure for those companies that have appropriate impact measurement methods in place. However, many companies just re-label more of their products as being sustainable without having much of an impact.

Focus on share-based performance

Equity-linked compensation is widely considered to be an effective means to align the interests of managers and shareholders, and yet this can only be achieved if the equity plan is adequately structured. We continue to see companies that have poorly designed stock plans which fail to incentivize executives to focus on delivering long-term, sustainable performance. For instance, some companies choose to grant their CEOs long-term incentive awards which are predominantly in the form of time-based equity. We consider it best practice for a majority of an executive's long-term incentive award to be in the form of equity vesting based on performance against pre-set quantifiable targets set over a multi-year period.

In addition, stock options with no performance conditions attached continue to represent a disproportionately large portion of many CEOs' pay packages. We view this as a concern. We favor the use of stock compensation as opposed to stock option compensation, as stock options have been shown to incentivize risk-taking behavior, given that they provide limited downside risk and significant upside potential.

Share ownership guidelines for executives are another important feature of an adequately designed compensation plan. These are meant to ensure that executives build and maintain a meaningful level of stock ownership throughout their tenure, thereby ensuring that manager and shareowner incentives are aligned. Hence, during our conversations, we continue to focus on ensuring that adequate ownership guidelines are in place for executives.

Pay ratios

When analyzing the size of the compensation paid to executive directors, we not only assess the absolute value of the remuneration package, but also how this compares to the company's wider workforce. Investors often use pay ratios to compare top and bottom salaries within an organization. The most popular ratio is the CEO pay ratio, which was introduced by the Dodd-Frank Wall Street Reform and Consumer Protection Act and is calculated by dividing the CEO's remuneration with the pay of the median employee.

Before the pandemic, it had already been established that these ratios were increasing. However, the disrupting characteristics of the pandemic have exacerbated global income inequality through issues such as lost income and rising inflation, both of which have a significantly higher impact on lower-income groups. As a result, and in the pursuit of reversing the increase in global income equality, we expect investors to pay increasingly more attention to the relative pay levels of company executives.

Structure and oversight

Remuneration oversight remains a focal point of our engagement. We focus on ensuring that the committee responsible for remuneration is sufficiently independent so as to provide objective decision-making in the interests of shareholders. In addition, we view it as best practice for companies to engage with shareholders to gain feedback on their pay practices and to thereby set up a process of improving remuneration practices on a continuous basis.

When there is significant dissent on remuneration-related voting items, we expect companies to initiate a dialogue with shareowners to identify what factors prompted the opposition, and to determine what changes to the pay policies and/or practices are needed. We also pay particular attention to whether companies provide clear and transparent disclosure with regards to any instances where discretionary adjustments to pay outcomes or structures are rolled out. Notably, we assess whether the body responsible for remuneration matters adequately discharged its oversight responsibilities by ensuring that an appropriate remuneration structure is in place. ■

CASE STUDY

TESCO

We have been engaging with UK retailer Tesco on executive remuneration since 2020, when the company's remuneration report was rejected by a majority of the votes cast at the AGM during that year. The company has rolled out meaningful improvements to its compensation plan since we initiated our dialogue. Most recently, Tesco revised its remuneration policy and included ESG metrics in the executive pay design while also simplifying the structure of its short-term incentive plan.

WOLTERS KLUWER

Wolters Kluwer has undergone significant changes over the last several years, having finalized their transition into a digital solutions company. To facilitate this transition, the company has had to adapt some of their corporate governance practices on executive remuneration. The CEO of Wolters Kluwer has historically received excessive payouts compared to local benchmarks and industry peers. This is in part due to retaining and attracting talent from markets with above average executive pay like the US, as well as incentivizing stability throughout the company's long-term transition. In response to continuous shareholder feedback on the excessive payouts, the company has reduced the maximum opportunity under the long-term incentive plan from 285% to 240% of base salary.

Proxy Voting

DIANA TRIF – *Engagement specialist*
LUCAS VAN BEEK – *Active ownership analyst*

Engagement specialist Diana Trif and active ownership analyst Lucas van Beek reflect on some of the recent trends in proxy voting, from the increased scrutiny among investors around companies' board elections to the recent legislative changes around submitting shareholder proposals in the US.

Increased scrutiny on Board Elections

Board elections, the process in which investors have the right to elect directors to the company's Board of Directors during shareholder meetings, have consistently been one of the fundamental aspects of corporate governance. Corporate boards are responsible for sufficient oversight and can act as a sounding board for management by providing insights and foresight on directors' relevant fields of expertise. Good corporate governance is defined by distinct responsibilities between executive and non-executive directors, with board committees delving into specific matters that require more time and resources. Global best practice requires corporate boards to have sufficient independence levels, both overall and within separate board committees, while safeguarding a relevant and diversified set of skills, expertise, and experience amongst directors to reflect all stakeholders' perspectives.

Historically, there has not been much scrutiny around the election of board directors. Especially not in the absence of a proxy contest or dedicated campaign to vote Against certain directors. Often investors went along with management's recommendations as the majority of board elections are considered routine items at companies' annual general meetings (AGMs). However, over the past years we have witnessed a rise in interest from the public as to how investors use their voting rights, which along with other trends resulted in increased scrutiny from shareholders regarding board elections. First of all, this means investors are increasingly demanding the possibility to hold individual directors accountable. This is for instance not possible in the case of a slate election method, where board directors are jointly put forward in one list (a slate). Secondly, investors continue to prefer the ability to re-elect directors on an annual basis, which is not the case when the election frequency is set to more than one year or when a board is staggered, meaning that only a rotating part of the board is eligible for (re-)election.

Besides investor preferences regarding the different election types and frequencies, director opposition by shareholders has increased over the past couple of years. The 2022 proxy voting report by Semler Brossy showed that the percentage of directors from Russel 3000 companies receiving less than 95% support rates from investors has increased from 22% five years ago to 30% in 2022. Insufficient board independence, gender diversity concerns or potential overcommitment, have been standard drivers of voting Against a director's election. However, nowadays shareholders use the election of board directors to signal discontent around broader topics like environmental and social concerns.

In 2020, Robeco introduced a policy to vote Against the nomination of the most accountable board member for companies in high carbon emitting sectors that do not sufficiently address the impact of climate change. This year, we introduced a similar policy related to human rights, identifying and voting Against the election of the most accountable board member for companies that face significant human rights issues and are linked to social controversies, while performing insufficient due diligence regarding their human rights impacts. Robeco has also been signaling its discontent regarding some companies' persistent unacceptable remuneration practices by voting Against the Chairs of their remuneration committee for multiple years now. Finally, we expect shareholders to carry on showing their increased scrutiny of corporate actions, by opposing relevant agenda items such as the re-election of a board member, and we aim to continuously broaden our policies both in terms of scope and themes.

Market developments in the United States

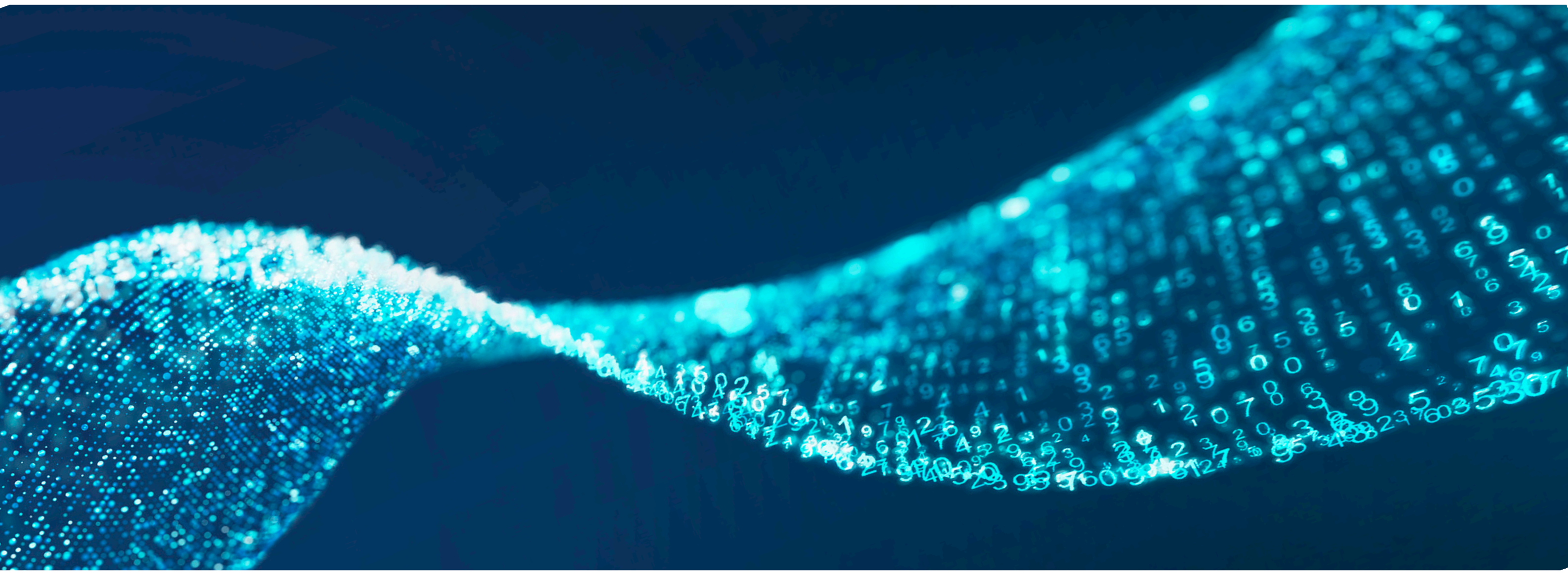
The US is often cited as a model of good governance characterized by a focus on shareholder rights and robust disclosure requirements. The US corporate governance model is, however, far from being a static system. In the past decades, it has undergone significant changes. These changes were spurred by the accounting scandals of the early 2000s and the 2008 financial crisis, which directed significant scrutiny towards public company boards and raised awareness regarding the far-reaching impacts of poor corporate governance. The Covid-19 pandemic, climate change, and the increase in global wealth and income inequality have again dramatically reshaped the corporate governance landscape. Investors have increased their expectations and are using their rights more than ever to hold companies accountable. Against this backdrop, regulators continued to roll out initiatives to reform the corporate governance system to adapt to these new realities.

One major change that was recently rolled out in the US was the Securities and Exchange Commission's (SEC) adoption of new rules requiring that all companies use 'universal proxy cards' for any meetings involving contested elections. The new rules, which apply to shareholder meetings after August 31, 2022, will overhaul the mechanisms by which proxy contests have been carried out in the US thus far. Prior to the amendments, shareholders voting by proxy were unable to 'mix and match' nominees put forward by the incumbent board and the dissident shareholder, as they could if voting in person. These shareholders were therefore faced with a binary choice – to vote either for one slate or the other, resulting in no or sweeping change. The new rules require both the incumbent board and the dissident shareholder to provide shareholders with a slate including the names of all dissident and registrant nominees, allowing shareholders voting by proxy to choose nominees from either side. We welcome this change as it places investors voting in person and by proxy on equal footing.

In a separate initiative, the SEC proposed certain amendments to Rule 14a-8, which governs the process by which shareholder proposals are included in a company's proxy statement. Under this rule, a company may omit a shareholder proposal from its proxy statement if the proposal falls within one of 13 substantive bases for exclusion. The proposed amendments focus in particular on the substantial implementation, duplication, and resubmission of proposals, aiming to "improve the shareholder proposal process and promote consistency." In recent years, the current rules drew criticism over concerns that the existing standards for exclusion were not consistently implemented, thereby leading to unpredictable outcomes. The new rules address these concerns by ensuring a more transparent framework for the rule's application. We support the changes and expressed our position by participating in the public consultation launched by the SEC on the new rules.

Another development we are closely following is the California Gender Board Diversity Law. In May 2022, the California law requiring increased female representation on public company boards headquartered in the state was struck down. The decision came weeks after a court invalidated a bill requiring California-based publicly listed corporations to have board members from underrepresented communities. This outcome prompted concerns that the rulings will stifle future efforts to enact diversity regulations in the US. Despite this, companies continue to face mounting pressure from shareholders to increase diversity in the boardroom. At the same time, the Nasdaq Board Diversity Rules, which became effective in August 2022, signal that the focus on diversity remains ongoing and that companies should continue striving to ensure an adequate level of board diversity. ■

CODES OF CONDUCTS



Robeco's Engagement Policy

Robeco actively uses its ownership rights to engage with companies on behalf of our clients in a constructive manner. We believe improvements in sustainable corporate behavior can result in an improved risk return profile of our investments. Robeco engages with companies worldwide, in both our equity and credit portfolios. Robeco carries out two different types of corporate engagement with the companies in which we invest; value engagement and enhanced engagement. In both types of engagement, Robeco aims to improve a company's behavior on environmental, social and/or corporate governance (ESG) related issues with the aim of improving the long-term performance of the company and ultimately the quality of investments for our clients.

Robeco adopts a holistic approach to integrating sustainability. We view sustainability as a long-term driver of change in markets, countries and companies which impacts future performance. Based on this belief, sustainability is considered as one of the value drivers in our investment process, like the way we look at other drivers such as company financials or market momentum.

More information is available at: https://www.robeco.com/docm/docu-robeco-engagement-policy.pdf

The UN Global Compact

One of the principal codes of conduct in Robeco's engagement process is the United Nations Global Compact. The UN Global Compact supports companies and other social players worldwide in stimulating corporate social responsibility. The Global Compact became effective in 2000 and is the most endorsed code of conduct in this field. The Global Compact requires companies to embrace, support and adopt several core values within their own sphere of influence in the field of human rights, labor standards, the environment and anti-corruption measures. Ten universal principles have been identified to deal with the challenges of globalization.

Human rights

1. Companies should support and respect the protection of human rights as established at an international level
2. They should ensure that they are not complicit in human-rights abuses.

Labor standards

3. Companies should uphold the freedom of association and recognize the right to collective bargaining
4. Companies should abolish all forms of compulsory labor
5. Companies should abolish child labor
6. Companies should eliminate discrimination in employment.

Environment

7. Companies should adopt a prudent approach to environmental challenges
8. Companies should undertake initiatives to promote greater environmental responsibility
9. Companies should encourage the development and diffusion of environmentally friendly technologies.

Anti-corruption

10. Companies should work against all forms of corruption, including extortion and bribery.

More information can be found at: https://www.unglobalcompact.org/

CODES OF CONDUCTS

OECD Guidelines for Multinational Enterprises

The OECD Guidelines for Multinational Enterprises are recommendations addressed by governments to multinational enterprises operating in or from adhering countries, and are another important framework used in Robeco's engagement process. They provide non-binding principles and standards for responsible business conduct in a global context consistent with applicable laws and internationally recognized standards.

The Guidelines' recommendations express the shared values of the governments of countries from which a large share of international direct investment originates and which are home to many of the largest multinational enterprises. The Guidelines aim to promote positive contributions by enterprises to economic, environmental and social progress worldwide.

More information can be found at: http://mneguidelines.oecd.org/

International codes of conduct

Robeco has chosen to use broadly accepted external codes of conduct in order to assess the ESG responsibilities of the entities in which we invest. Robeco adheres to several independent and broadly accepted codes of conduct, statements and best practices and is a signatory to several of these codes. Next to the UN Global Compact, the most important codes, principles, and best practices for engagement followed by Robeco are:

– International Corporate Governance Network (ICGN) statement on
– Global Governance Principles
– United Nations Global Compact
– United Nations Sustainable Development Goals
– United Nations Guiding Principles on Business and Human Rights
– OECD Guidelines for Multinational Enterprises
– Responsible Business Conduct for Institutional Investors (OECD)

In addition to our own adherence to these codes, we also expect companies to follow these codes, principles, and best practices. In addition to our own adherence to these codes, we also expect companies to follow these codes, principles, and best practices.

Robeco's Voting Policy

Robeco encourages good governance and sustainable corporate practices, which contribute to long-term shareholder value creation. Proxy voting is part of Robeco's Active Ownership approach. Robeco has adopted written procedures reasonably designed to ensure that we vote proxies in the best interest of our clients. The Robeco policy on corporate governance relies on the internationally accepted set of principles of the International Corporate Governance Network (ICGN). By making active use of our voting rights, Robeco can, on behalf of our clients, encourage the companies concerned to increase the quality of the management of these companies and to improve their sustainability profile. We expect this to be beneficial in the long term for the development of shareholder value.

Collaboration

Where necessary, Robeco coordinates its engagement activities with other investors. Examples of this includes Eumedion; a platform for institutional investors in the field of corporate governance and the Carbon Disclosure Project, a partnership in the field of transparency on CO_2 emissions from companies, and the ICCR. Another important initiative to which Robeco is a signatory is the United Nations Principles for Responsible Investment. Within this context, institutional investors commit themselves to promoting responsible investment, both internally and externally.

Robeco's Active Ownership Team

Robeco's voting and engagement activities are carried out by a dedicated Active Ownership Team. This team was established as a centralized competence center in 2005. The team is based in Rotterdam, the Netherlands, and Hong Kong. As Robeco operates across markets on a global basis, the team is multi-national and multi-lingual. This diversity provides an understanding of the financial, legal and cultural environment in which the companies we engage with operate. The Active Ownership team is part of Robeco's Sustainable Investing Center of Expertise headed by Carola van Lamoen. The SI Center of Expertise combines our knowledge and experience on sustainability within the investment domain and drives SI leadership by delivering SI expertise and insights to our clients, our investment teams, the company and the broader market. Furthermore, the Active Ownership team gains input from investment professionals based in local offices of the Robeco around the world. Together with our global client base we are able leverage this network to achieve the maximum possible impact from our Active Ownership activities. ■

ROBECO

Robeco Institutional Asset Management B.V. (Robeco) is a pure play international asset manager founded in 1929. It currently has offices in 15 countries worldwide and is headquartered in Rotterdam, the Netherlands. Through its integration of fundamental, sustainability and quantitative research, Robeco is able to offer institutional and private investors a selection of active investment strategies, covering a range of asset classes.

Sustainability investing is integral to Robeco's overall strategy. We are convinced that integrating environmental, social and governance (ESG) factors results in better-informed investment decisions. Further we believe that our engagement with investee companies on financially material sustainability issues will have a positive impact on our investment results and on society.

Please visit Robeco website for more information.

IMPORTANT INFORMATION

ROBECO
The Investment Engineers

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