Cassels

Continued Focus on ESG Issues by Proxy Advisory Firms for 2023 Proxy Season, including "Say on Climate"

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As we are advancing in the 2023 proxy season, environmental, social and governance (ESG) matters continue to be at the forefront for proxy advisory firms, such as Institutional Shareholder Services (ISS) and Glass Lewis & Co. (GL). Relevant ESG factors include, but are not limited to, climate change, human capital management, diversity, stakeholder relations, and health, safety, and environmental matters. Therefore, it is essential for issuers to keep ESG-related matters and risks top of mind and to fully explain all relevant and material factors in continuous disclosure filings and materials prepared for shareholders. Not only could insufficient management of ESG issues, or insufficient disclosure thereof, result in a negative voting recommendation from ISS and GL but, more importantly, such issues may present legal, financial, and reputational risks.

Say on Climate

"Say on Climate" (SoC) votes are gaining traction in the Canadian market, and it will be interesting to see how this trend continues to evolve for the 2023 proxy season. Say on Climate is modelled on *"Say on Pay" votes*, and involves shareholders casting a non-binding advisory vote on an issuer's climate policies. The SoC concept has three components: first, issuers must annually disclose their greenhouse gas (GHG) emissions; second, issuers must disclose a plan to manage these emissions; and lastly, shareholders are provided the opportunity to approve or disapprove the plan and performance of the issuer. SoC can take the form of management-supported, where the management team themselves implement SoC with the support of their board of directors. These resolutions establish a policy for mandatory disclosure of GHG emissions, their climate action plan, and an annual vote at future AGMs. SoC can also come in the form of a shareholder proposal, urging management to implement a SoC vote.

Although this is still in its early stage, ISS has developed guidance regarding SoC and suggests that votes will be recommended on a case-by-case basis. With respect to management proposals, the ISS guidelines state that ISS will, among other things, consider: (i) the completeness and rigor of the plan considering the issuer's disclosure of its operational and supply chain GHG emissions; (ii) whether the issuer discloses a commitment to report on the implementation of its plan in subsequent years; and (iii) the extent to which the issuer's climate related disclosures are in line with Task Force on Climate-related Financial Disclosures (TCFD) recommendations. ISS will also vote case-by-case on shareholder proposals that request the issuer to disclose a report providing its GHG emissions levels and reduction targets.

To date, GL does not have a specific policy addressing SoC vote within their guidelines. However, GL's website provides an overview of the GL approach to SoC. This overview indicates that this issue is still very much flux, and likely will be throughout the proxy season. Given the broad variety of proposals – both management and shareholder proposals – and the lack of standardization on how shareholders should evaluate each of the climate plans submitted to a vote, GL will continue to maintain a case-by-case approach on this issue, although GL indicates that it will generally recommend against both management proposals and shareholder proposals requesting that issuers adopt a policy that provides shareholders with an annual SoC vote on a plan. However, when issuers bypass this step, and place their climate plans up for an advisory vote, GL will evaluate these climate plans on a case-by-case basis.

The benefits of such a vote include accountability and ensuring that issuers are producing robust, TCFD-aligned disclosures that should allow shareholders to understand how each company is considering climate in its long-term strategy. But there have also been concerns raised by investors with regards to the SoC, namely that such an approach limits board accountability for climate strategies, and that if these plans become routine, investors may become passive and approve practices of substandard issuers.

What is clear, is that SoC votes will continue to be a trend that should be closely monitored during the 2023 proxy season.

Other ESG related highlights from ISS and GL's proxy voting guidelines for the 2023 proxy season include...

Diversity

GL has transitioned from a numerical approach with respect to gender diversity to a percentage-based approach for upcoming shareholder meetings. GL will recommend voting “against” (or “withhold”) with respect to the Nominating Committee Chair of any TSX issuer where the board is not at least 30% gender diverse, as well as all members of the Nominating Committee of a TSX issuer board with no gender diverse directors.

Similarly, with respect to S&P/TSX Composite Companies, ISS will recommend to generally vote “against” (or “withhold”) with respect to the Nominating Committee Chair or Board Chair where women comprise less than 30% of the Board. ISS guidelines additionally state that, as of February 1, 2024, ISS may generally vote “against” (or “withhold”) with respect to the Nominating Committee Chair where the Board has no apparent racially or ethnically diverse members.

Cyber Risk Oversight

GL has implemented a new section into their guidelines regarding cybersecurity disclosure and have indicated that oversight concerning cyber-related issues is paramount. As a result, GL may recommend against directors where cyber-attacks have caused significant harm to shareholders and the issuer's disclosure, or oversight, is insufficient addressed.

Climate Related Issues

The guidelines of GL and ISS highlight that an ESG priority in the 2023 proxy season relates to climate change. Both GL and ISS issued amendments to their guidelines with respect to issuers whose greenhouse gas (GHG) emissions represent a financially material risk or are significant GHG emitters respectively. GL and ISS will recommend voting against a member of the Board where the issuer has not provided Task Force on Climate-related Financial Disclosures (TCFD)-aligned climate-related disclosure. GL states that Boards should have clearly defined board oversight responsibilities.

Director Commitments and Over-boarding

Both GL and ISS again comment for 2023 meetings on the over commitment of directors within their guidelines.

GL recommends shareholders oppose the election a director who is: (i) executive officer of a public company while serving on more than one additional public company board; (ii) executive chair/vice chair of a public company while serving on more than two additional public company boards; or (iii) serving as a non-executive director on more than five public company boards in total.

Similarly, ISS recommends shareholders vote withhold for director nominees at TSX Companies and Venture-Listed Companies who: (i) are non-CEO directors and serve on more than five public company boards; or (ii) are CEOs of public companies who serve on more than two additional public company boards.

These are just some of the highlights in the updated 2023 guidelines from GL and ISS. The ESG team at Cassels has significant experience assisting clients in preparing for, and dealing with, these guidelines and would be happy to answer further questions about the ESG-related requirements for the 2023 proxy season.
