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CEOs Can't Ignore These Three Proxy Season Votes

By **Thomas Singer** - October 13, 2017

When reviewing this year's proxy season, one takeaway looks certain to grab CEOs by the ear: The tremendous enthusiasm for environmental and social issues.

The share of proposals on environmental and social issues (E&S) climbed to 43% – the highest in five years. Moreover, actual passage levels have risen. In 2017 so far, six proposals passed; in all of 2013 just four passed.

While the intensity of support should matter to CEOs, so should the sources of support. These issues no longer receive backing from just active investors – the usual suspects. A growing body of large, traditionally passive investors put many of these recent proposals over the goal post. After all, they deem these issues' outcomes essential to shareholder value.

CEOs, take notice: the following three E&S topics gained serious momentum, which looks all but certain to continue.

> **"A LACK OF DIVERSITY ON THE BOARD CAN ACT AS A WARNING SIGNAL FOR INVESTORS, AMONG OTHER REASONS BECAUSE IT CAN EXACERBATE GROUPTHINK."**

In this year's proxy season, proposals on climate risk disclosure reached a record level of support: an average backing of nearly 40% of votes cast. 2016 saw a backing of 28% and in 2015 just 17%.

CEOs wanting to make headway can consider looking to Alcoa. While most companies stay mum on how climate-related risks may affect them, Alcoa's annual report extensively details the potential impacts climate change could have on their operation. Impacts range from costs associated with regulation to operational impacts resulting from changes in rainfall patterns and water shortages. The report makes clear that, if these impacts materialize, they will damage the company's production and financial performance.

Climate Risk Reporting

Rather than wait for shareholders to voice their frustration, CEOs can act preemptively. To make climate risk reporting a reality, they can drum up support with internal constituencies – especially corporate secretaries, CFOs, and government relations officers. Given the abundant research and other warning signs, executives can make the economic case with more confidence than ever. The World Economic Forum, for instance, has ranked "extreme weather events" among the top two global risks in each of the last four years. And now, even large, passive investors like BlackRock and Vanguard have begun flagging this issue.

Board Diversity

This year, the volume of proposals on diversity almost tripled compared to last year. Fourteen proposals came to a vote in 2017 – up from five in 2016. The majority of proposals, two of which passed, pertained to what steps companies should take to improve board diversity.

CEOs with low female representation on their boards are facing increasing scrutiny from shareholders and society. A lack of diversity on the board can act as a warning signal for investors, among other reasons because it can exacerbate groupthink. Adding gender diversity (or any other kind of diversity) can go a long way to improving the collective decision-making of a board.

To accelerate progress, CEOs can consider the “Every Other One” approach. Coined by the Committee for Economic Development, the approach entails appointing a woman to every other vacant board seat. By doing so while retaining existing female directors, over the next five years women would comprise about a third of seats in the Fortune 500 and Fortune 1000 – a good start given that women currently hold only about one out of five seats.

CEOs can also advocate that their boardroom nominating committees cast broader nets. Often, companies seek out just current or former CEOs for their boardrooms, which prevents countless qualified women from consideration. A robust pool of qualified women candidates might include division presidents, chief human resource officers, management consultants, and entrepreneurs.

Sustainability Reporting

In 2017, proposals asking companies to publish a sustainability report attracted record-high backing: average support clocked in at nearly 32% of votes – up from 26% in 2016. These proposals call for companies to publish annual reports disclosing their performance on various non-financial impacts, such as energy and water consumption, emissions, health, human rights, and safety.

For CEOs who have put this exhaustive effort on the backburner, it may mean taking a second look at the upsides. Done well, sustainability reporting can reveal opportunities for new revenue and innovation – two benefits no leader can ignore. The whole exercise of compiling, analyzing, and reporting non-financial data can shed light on operational inefficiencies as well as market opportunities. In part, this is how companies as diverse as Philips and Johnson & Johnson have built $10 billion-plus portfolios on the backbone of sustainability.

Also, CEOs who prioritize sustainability reporting now may save their companies time and effort down the road. There are more and more instances of sustainability reporting becoming an actual requirement. It already applies to companies operating in the EU, and those listed across a dozen global stock exchanges. Rather than waiting for the next mandate to happen and risk throwing companies into a tizzy, executives can take a preemptive approach now.

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