Categories: Hot Topics > Data & Disclosure | Institutions > Pension funds | Institutions > Asset Managers | Institutions > Companies | Institutions > Civil society | Environmental > Climate change | Governance > Voting & engagement

Investors challenge ISS over 'inadequate' response to climate in planned voting advice for 2022

Letter by $2trn investor coalition sent as SEC proposes changes to rules around proxy advice and adopts 'universal' proxy card rule for contested director elections

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Investors in Europe and the US have written to influential proxy advisor ISS expressing concern over how it plans to approach climate risk in its voting advice next year.

ISS has just wrapped up a consultation with the market on its 'benchmark policy' for 2022, which will outline the position it will take on key votes and topics in the coming proxy season in its main advice.

To coincide with the end of the feedback period, more than 30 investors including Quilter, Unigestion and EOS - the stewardship services arm of Federated Hermes - have penned a letter saying the coverage of climate risk in the policy is "inadequate given the severity of the climate crisis".

The investors' letter, addressed to ISS' President and CEO Gary Retelny, argued that "the failure to meaningfully incorporate a company's alignment with a 1.5°C scenario into proxy recommendations may lead ISS to make recommendations that are not in the best interests of shareholders".

The group urges ISS to make a number of changes to the plans before the final guidelines are published in coming weeks, including a commitment to recommend votes against directors at companies failing to manage or mitigate "ESG risks" by "fail[ing] to align business plans, capital allocation, and policy influence (political spending and direct/indirect lobbying activities) with a 1.5°C scenario".

It asks ISS to "expand and disclose" its analysis of companies on such issues, and to support all climate-based proposals "unless the company has demonstrated meaningful alignment of its business activities with 1.5°C scenario".

ISS surveyed the market on climate change for the first time in August, ahead of drafting its benchmark policy for 2022. However, Marcela Pinilla, Director of Sustainable Investing at SRI firm Zevin Asset Management - one of the letter's signatories - expressed concerns that 46% of respondents were understood to be companies whose views "might be at odds" with that of investors.

This was echoed by another signatory, Lauren Compere, Director of Shareholder Engagement at Boston Common Asset Management, who questioned the "almost equal voice" companies had in the consultation.

"I think we should have priority in terms of what we're seeking as clients of ISS," she said, adding that, as the largest proxy advisor in the world, ISS "really sets the global standard". "What they do can really impact how others look at this issue".

A spokesperson for ISS told RI that the firm is "mindful that climate risk is an important and fast-moving topic engendering strong views among institutional investors, their portfolio companies, and market participants more broadly".

"ISS has and continues to actively engage with clients and numerous other stakeholders as part of our policy review process which includes, but is not limited to, this year's inaugural survey dedicated to climate and multiple discussions with a broad cross-section of investors and investor organizations on this important issue," he said.

The investor letter comes the same week that the US Securities and Exchange Commission (SEC) has proposed to rescind Trump-era rules requiring proxy advisors to share their advice with companies ahead of their annual meetings and votes.

The rules, introduced last year, also required advisors to notify clients of any responses from the firms, and drew the ire of many investors who argued they impinged on the independence of proxy advice and impaired the timeliness of its delivery.

Yesterday, three out of five of the Commissioners at the powerful US regulator voted in favour of the proposal to overturn them, which will now go to a 30-day public comment period.

"Proxy advice voting businesses play an important role in the proxy process. Their clients deserve to receive independent proxy voting advice in a timely manner," said SEC Chair, Gary Gensler.

Republican Commissioner Hester Pierce, however, voted against the proposal, arguing that the Commission "lacks a sound basis for seeking to amend a brand new rule".

"Nothing has changed since we adopted the rule, and we have not learned anything new. The release takes a stab at justifying the rewrite, but we might as well simply acknowledge that the political winds have shifted," she said.

Sarah Wilson, CEO at UK-based proxy advisor Minerva Analytics told RI that she very much welcomed the SEC's decision to "review and scale back the previous administration's proposals".

"Contrary to assertions from some of the Commissioners, the initial rules process was deeply flawed," she said.

At the same time, the SEC also introduced rules which will allow shareholders to vote for their preferred mix of candidates in cases where a company's board is being contested, such as the recent Engine No.1 activist campaign at Exxon.

The new 'universal' proxy card ruling means all directors up for election, including those put forward by shareholders, will be given the same status in a vote by being included in a single document.

Previously, shareholders who voted remotely in contested elections had to choose from a full slate of board directors nominated by the management or a competing set of nominees provided by an activist investor – as was the case at Exxon this year.

The new rule, which was supported by four SEC Commissioners, comes into effect in August 2022.

"Today's amendments will put these candidates on the same ballot. They will put investors voting in person and by proxy on equal footing. This is an important aspect of shareholder democracy," said SEC's Gensler.

tagged with: ISS, SEC, Minerva, Proxy Advice