Association of Member Nominated Trustees

A 2021 update on fund managers' voting policies on climate change

About

Association of Member Nominated Trustees

> ABOUT THE AMNT

The Association of Member Nominated Trustees (AMNT) was established in 2010 as an organisation run by and for member nominated trustees, directors and representatives of private sector and public sector pension schemes. AMNT has more than 850 individual trustee members, representing pension schemes with assets under management of over £1-trillion.

> ABOUT THE AUTHOR

Leanne Clements was AMNT's Campaign Manager for Red Line Voting from March 2017 to September 2021. Leanne was responsible for supporting the adoption and implementation of Red Line Voting policies by working with AMNT and its members, fund managers, policy makers as well as other important actors in the investment chain. Prior to this role, Leanne led the responsible investment strategies at three different UK pension schemes. Prior to that, she worked at a corporate governance and shareholder advisory consultancy, most notably conducting voting policy generation and executing voting instructions for UK pension schemes. Prior to her career in the UK, she worked in her native Canada as an environmental consultant for an engineering firm conducting contaminated site investigations for financial clients.

Red Line Voting

> ABOUT THE RED LINE VOTING INITIATIVE

The AMNT supports the view that trustees should be adopting active stewardship policies covering environmental, social and corporate governance (ESG) matters and as a result, should be allowed to direct how their votes are cast at shareholder meetings of the companies in which they invest, at the very least on a comply-or-explain basis.

Red Line Voting is the UK's first comprehensive template policy for investors covering the range of ESG issues. It was developed over two years by AMNT with very substantial consultation with the fund management industry, proxy voting companies, market analysts, investment consultants and of course pension scheme trustees and executives. It was sparked by the 'shareholder spring' of 2012 when pension scheme trustees attempted to use their votes in the revolt against excessive executive pay. The trustees – of small to fairly large schemes – discovered that they were unable to do so: they were told that as they invested in pooled funds their votes were under the control of the fund managers.

AMNT considered this to be unacceptable and, since the investment industry explained that this was so because there was no trustee demand to use their votes and in any case it was difficult to vote different voting policies, resolved to develop a voting policy for trustees that they could put forward. The Red Lines were designed to make it easier for the fund management industry to respond to trustee ESG policies. If many trustee boards adopted these policies then the fund managers would be able to operate one collective policy for all those clients. The policies did not dispense with the need for fund managers to use their expertise and judgement - far from it. AMNT made clear our expectation that fund managers should engage with companies as per usual but on the basis of the Red Lines, and then use their judgement to decide whether the company's performance in this regard merited the prescribed voting action. The fund managers are at liberty to vote contrary to the Red Lines if they judged that course of action to be in the clients' best interests, and if they did they were required to explain their reasoning to their clients.

One of the benefits for trustees to use Red Line voting policies is that it covers a wide range of environmental and social issues, in addition to the more traditional governance issues covered by most publicly available voting policies in the market. In June 2021 the Red Lines were updated and the new policies include a suite of new voting policies on climate change.

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› Executive Summary

In 2019 when AMNT conducted its first review of fund managers' policies it was in the light of trustees being faced with regulatory and Parliamentary pressure to improve their stewardship of their assets on the one hand, but the refusal of fund managers to enable trustees to fulfil these requirements and expectations by accepting and respecting trustees' voting policies on the other.

> "
> **Trustees had been told that they should leave stewardship to the fund managers as they have the resources and expertise to develop voting policies. They were also told that if clients do not like their fund manager's stewardship approach, they should take their business elsewhere.**
> "

This provoked several questions including:

- How did fund managers' voting policies compare to AMNT's Red Line Voting policies, which cover ESG considerations and are derived in the main from the UN Global Compact and UK Corporate Governance Code?
- How publicly transparent were fund managers on their voting policies? Was there sufficient information in the public-domain, presented sufficiently clearly, such that an asset owner, seeking to benchmark a fund manager's voting policy against its own during the selection process, can conduct an effective comparative analysis?
- How much variation is there in voting policy across the fund management industry? Is there in fact any real consumer choice?

AMNT therefore conducted a survey of major fund managers to establish the answers to these questions.

Two years on, there is even more regulatory pressure on trustees to develop their own voting policies. There has been some limited movement in the market with the introduction of a new fund that gives trustees a choice of voting policy including the AMNT's Red Lines . However we are fully aware of the continued reluctance of most major fund managers to accept trustees' voting policies. So the questions asked in our 2019 review remain relevant today. Thus, AMNT conducted a second review into fund manager voting policies and guidelines on climate change to answer these questions again.

In June 2021, AMNT updated its Red Line Voting policies for climate change in several key areas and these form the basis of the 2021 survey. The new policies and guidelines cover five key areas:

- Board level responsibility for climate change, not merely environmental issues
- Disclosure of climate change approach against TCFD
- Paris-aligned strategy and science-based targets (not targets or emission reductions with no qualifier that they need to be Paris-aligned/net zero/science based).

> Remuneration metrics which specifically reference climate change

> Climate change lobbying, including full disclosure of company lobbying activities on climate.

Thirty fund managers' voting policies were compared with these updated Red Lines under six categories (strategy and targets were split into two separate categories). Stewardship reports and voting records were not given credit as this study was focussed on voting policies and guidelines, not outcomes. Separate online documents that contain information on climate change with no reference or hyperlink to them in the voting policy itself were also not given credit.

TERMINOLOGY:

As there appears to be no standardisation as to how voting policies and guidelines are defined, for the purposes of this report we define the terms as follows:

A **voting policy** can be defined as a description of the expectation that the fund manager has for an investee company regarding the ESG issue in question. It may also explicitly include the investment belief that the fund manager has. A **voting guideline** can be defined as a voting instruction that a fund manager will or may take subject to, for example, engagement outcomes.

Note that some fund managers having voting policies and guidelines, voting policies only or voting guidelines only. For those fund managers who only have **voting guidelines,** credit will be given for having a voting policy if the voting guidelines are described in such a way that the specific requirements stated in the review methodology and Appendix A are met.

KEY FINDINGS ON VOTING POLICY:

1. 40% of the fund managers (12/30) either:

   > Did not disclose their voting policy on any ESG issue; or

   > Did not reference climate change in their voting policy at all; or

   > Referenced climate change but none of their references met AMNT's Red Line voting policies on climate and thus reasonable standards for taking action on climate change.

2. Of the remaining fund managers, the number of fund managers that met AMNT's individual policies on climate change was quite low (a little over half for TCFD and for the remaining categories 40% or less), and thus do not have reasonable standards for taking action on climate change.

3. Neither of the dominant proxy advisors - ISS or Glass Lewis - have voting policies and guidelines for climate change that reflected AMNT's policies, and thus reasonable standards for taking action on climate change

   This is a surprising find given the market and regulatory framework in which the UK is currently operating, especially if the UK government wishes to be a global leader on green finance. The four fund managers that met AMNT's policies on climate change demonstrate that there is no sufficient reason why the remaining fund managers are not at the same level.

   It is clear that language and terminology play an important role and must be addressed. Not explicitly referencing climate in board-level responsibility, or only stating "emissions reduction" is simply not sufficient in a post-Paris Agreement world; neither is the lack of references to Paris-aligned strategies and climate-linked remuneration.

KEY FINDINGS ON VOTING GUIDELINES:

> Only eight of the 30 fund managers reviewed would target directors for insufficient disclosure or action taken on climate change.

> Of those eight, only five of them would target the Chair.

> Of the 18 that had a voting guideline, nearly 40% of them only had a voting guideline for shareholder resolutions.

> Glass Lewis's voting guidelines covered only shareholder resolutions, and ISS made a cursory reference using weak language ("exceptional circumstances").

The significant percentage of fund managers whose voting guideline is only for shareholder resolutions is a significant concern for a financially material risk like climate change, because, if no shareholder resolutions are put forward at a company, the fund manager would not hold the company to account at all. In practice shareholder resolutions are rarely proposed. Glass Lewis, which covers more than 30,000 shareholder meetings, has reported that the total number of shareholder proposals they reviewed in 2020 was 434, of which just 17 concerned climate change.

Fund managers have justified the lack of or poor disclosure on voting guidelines on the grounds that they wished to maintain flexibility in their voting actions. Given that some fund managers are very clear and robust on how they will vote if their expectations are not met (e.g. LGIM, Federated Hermes), we see no reason why the other fund managers should be using the flexibility argument in 2021.

Even for those fund managers who do have a voting guideline, there are still residual issues remaining regarding the use of language. The first concerns terms used to describe their voting action regarding directors. A significant percentage of the fund managers use terms like "may withhold support", "we will consider voting against". However, as some fund managers have no difficulty in setting out clear statements it suggests that the flexibility argument does not hold true for every fund manager, and therefore it is possible to take a more robust stance on the issue, but the majority of fund managers choose not to.

The second issue concerns the lack of clarity over what may actually trigger the voting sanction. Terms like "insufficient disclosure or risk oversight" does not give sufficient information to determine the threshold that will trigger a vote of dissent. Fund managers should be held to account for both of these issues as it weakens the ability to scrutinise their approach. To be clear, AMNT supports the comply or explain principle when it comes to voting and engagement, and there are good reasons why a fund manager may choose not to take voting action against a company. But there is no reason why a fund manager cannot state what its default voting intention is if certain expectations are not met, and then provide an explanation through appropriate client reporting as to when they have deviated from that position and for what reason. This is the position we advocate.

Whilst we recognise that the fund manager has the ultimate responsibility for the contractual relationship between themselves and their proxy provider, the poor policies of the proxy voting companies in our view indicates a failure to recognise the gravity of the climate change crisis, particularly since fund managers (or indeed asset owners) lacking in responsible investment expertise and/or resources may choose to adopt their proxy agency's policy rather than develop their own.

CONCLUSIONS

Given how high climate change is on the regulatory agenda in the UK, it is very surprising that only four fund managers had a voting policy and guideline that met AMNT's criteria. It is clear that this issue requires urgent action, especially by the FCA as it relates to not only poor disclosure hindering market competition and the ability of trustees to make effective investment decisions, but also whether fund managers who refuse to accept AMNT's policy are doing what is necessary to tackle climate change in their approach to voting.

Lack of robust voting policies and guidelines: given market and regulatory developments since the Paris Agreement, AMNT expects fund managers to have:

> A voting policy on TCFD requirements, board level responsibility for climate change, Paris-aligned transition strategies, science-based targets, climate-linked remuneration, and climate lobbying.

> A voting guideline targeting directors (in addition to shareholder resolutions etc) for when the voting policy position is not met.

Time is running out to achieve the essential goals of keeping global warming well below 2 degrees and achieving net zero carbon emissions by 2050.

Lack of transparency by fund managers on climate-related voting hinders pension schemes from meeting their own climate related obligations. The whole voting chain, from investee companies to pension schemes – needs to reach this level of transparency and accountability. It only takes one investment actor to weaken the whole chain.

For those trustees who have identified climate change as financially material to their scheme, and wish to have their assets voted in a more robust way, where are they supposed to take their business given these findings? This issue is further exacerbated by the continued refusal of fund managers to accept client voting policies in pooled fund arrangements. Both our previous study, and this study, demonstrates that the trustees' Red Line policies on climate change are more effective than those of most fund managers, but currently most fund managers are insisting that trustees accept their inferior policies. It is for this reason that AMNT submitted their complaint to the Financial Conduct Authority in 2019.

It is crucial that fund managers are fully transparent on their voting policy and guideline on climate change so that investee companies and trustees know what to reasonably expect in advance of the Annual General Meeting, barring exceptional circumstances. A trustee should not be left in the dark as to how their fund manager intends to vote, especially if trustees are expected to hold their fund managers to account through benchmarking their own stewardship policies against that of their fund managers.

Voting policies versus outcomes

Some fund managers argue that they can demonstrate proof of their commitment to addressing climate change through their voting records and stewardship reporting. AMNT does not necessarily dispute their commitment; but demonstrating outcomes without disclosing their policy position on the issue gives no context to the outcomes that trustees – or advisors on their behalf – are reviewing. It also calls into question, rightly or wrongly, the commitment of the fund manager on the issue in question. An ad-hoc, case by case approach to addressing climate change is not an adequate policy stance for 2021.

Some fund managers provided AMNT with a lot of documentation on their approach to climate, how they engage with companies on climate, in separate documentation. None of this information however was contained within their voting policies. Trustees should not have to sift through the ESG/stewardship section of their fund managers' websites looking for information on their climate change approach. All voting policy and guideline-related information should be contained in one policy document.

RECOMMENDATIONS

Trustees

Trustees should work with their advisors to develop their own voting policy and guideline on ESG issues of material concern to their scheme. If climate change has been identified as one of their priority areas (and we would highly recommend its inclusion), we recommend that they adopt AMNT's RLV policies on climate change as outlined in this report. (Those of Aviva, BlackRock, LGIM and Federated Hermes are also good.) Trustees should request that their fund managers adopt these policies. If they refuse to do so the trustees should use the policies and the findings of this report to hold their fund manager to account if their voting policy and guideline does not align with their own policy. Collective pressure from trustees on these key issues is key to achieving real change in this area.

Fund managers

The fund management community should revaluate their voting policy and guidelines in advance of the 2022 proxy voting season and consider whether they are sufficiently clear and robust when compared to AMNT's Red Line climate change policies, and if not, make appropriate revisions to their policies accordingly.

Specific recommendations:

1. Voting outcomes and stewardship reporting should not be used to deduce a fund manager's stance on how they tackle climate change in their voting approach. Public disclosure of voting policies is equally important for complete accountability.

2. Expect investee companies to have climate change governance, strategy, and targets in alignment with TCFD recommendations, rather than merely asking companies to disclose against TCFD.

3. Expect investee companies to publicly disclose their Paris-aligned strategy and science-based/net zero targets

4. Tighten up the use of language with regard to emission reductions – state that the targets must be science-based or net zero.

5. Specify climate when referring to remuneration targets and lobbying activities.

6. Target company resolutions – ideally directors – to register a vote of dissent on climate rather than limiting voting action to shareholder resolutions on climate change. Be clear as to whom and under what specific circumstances the vote of dissent will be registered – avoid the use of "case by case" by clearly stating under what circumstances shareholder resolutions will be supported.

7. Ensure any additional material released on climate change is hyperlinked in the main voting policy document, where relevant.

Proxy voting agencies

Given their importance in the stewardship chain, we urge ISS and Glass Lewis to introduce explicit climate change voting policies and guidelines in alignment with AMNT's criteria.

Financial Conduct Authority

Given the FCA's own priorities regarding addressing "insufficient evidence of active stewardship in advancing environmental and social goals", the FCA's competition arm should seek regulatory action to remedy this market failure. This action would serve two important purposes:

> Allow trustees to have the necessary information to make appointment and retention decisions over the asset managers who will implement voting policies that reflect their priorities, and

> Ensure a more robust approach by the fund management community in tackling climate change in their voting approach.

Looking ahead

There are two major areas that investors should look to update their voting policies on climate.

1. Climate accounting

The main focus of investor analysis of company annual reports has been on the "front end" of the report, and not the profit and loss accounts at the "back end". It is just as important that the calculations and assumptions made in determining the financial health of the company take into account climate change. If the calculations and assumptions do not take into account climate change risks, this has a negative impact on capital allocation decisions, the share price of the company, what dividends shareholders receive, and so on. To date, climate accounting appears to have been largely ignored barring a few exceptions.

2. Testing corporate transition plans

Investors need to consider introducing more robust voting action if corporate transition plans are not in fact aligned with the Paris Accord. The gap in tools and expertise in measuring transition plans needs to be filled as soon as possible.

› 1. Introduction

In 2019 when AMNT conducted its first review of fund managers' policies it was in the light of trustees being faced with regulatory and Parliamentary pressure to improve their stewardship of their assets on the one hand but the refusal of fund managers to enable trustees to fulfil these requirements and expectations on the other by accepting and respecting trustees' voting policies. Trustees had been told that they should leave stewardship to the fund managers as they have the resources and expertise to develop voting policies. They were also told that if clients do not like their fund manager's stewardship approach, they should take their business elsewhere.

This provoked several questions:

> How many fund managers are in fact prepared to accept their clients' voting policies and operate split voting on pooled funds?

> How did fund managers' voting policies compare to AMNT's Red Line Voting policies, which cover ESG considerations and are derived in the main from the UN Global Compact and UK Corporate Governance Code?

> How publicly transparent were fund managers on their voting policies? Was there sufficient information in the public domain, presented sufficiently clearly, such that an asset owner, seeking to benchmark a fund manager's voting policy against its own during the selection process, can conduct an effective comparative analysis?

> How much variation is there in voting policy across the fund management industry? Is there in fact any real consumer choice?

AMNT therefore conducted a survey of major fund managers to establish the answers to these questions.

Two years on, there is even more regulatory pressure on trustees to develop their own voting policies. Towards the end of 2020 AMNT published a report that it had commissioned from Professor Iain Clacher into the barriers preventing trustees from directing the voting of their investments in pooled funds. Its key recommendation was for the Department for Work and Pensions to set up a taskforce to find a solution to these problems. We were delighted that Pensions Minister Guy Opperman welcomed the report and responded by establishing the Taskforce on Pension Scheme Voting Implementation, on which AMNT was represented.

The Taskforce produced its report in September this year. At the beginning of the year there had been limited movement in the market with the introduction of a new fund that gives trustees a choice of voting policy including the AMNT's Red Lines. It called this an "expression of wish". The key recommendation of the taskforce was that all pooled fund managers should follow that example and offer their clients an expression of wish.

The Financial Conduct Authority has since announced: "We agree with the Taskforce that there is no regulatory barrier to pension scheme trustees' issuing an 'expression of wish' to their asset managers regarding their voting preferences, and no breach of fund rules where a fund manager takes the expression of wish into account when voting.[1]" However, we are fully aware of the continued reluctance of most major fund managers to accept trustees' voting policies. So the questions asked in our 2019 review remain relevant today.

We believe that AMNT's Red Lines on climate change not only represent robust asset owner voting policies that should be respected by fund managers, but also a reasonable expectation on investee companies in 2021 given policy signals on the issue. Even if they don't accept client voting policies, fund managers' own voting policies on climate should at least be up to the same standard as AMNT's Red Lines. Therefore, our two main but connected drivers for completing this study were:

> Given the fund manager feedback on them being better placed to develop voting policies, to determine whether fund manager voting policies on climate change are better than asset owners' policies, using AMNT's Red Lines as the benchmark for that assessment

> Given that AMNT's Red Lines represent a reasonable expectation on investee companies vis a vis climate change, to determine whether or not fund managers are even meeting this reasonable standard and thus sufficiently taking action on climate change.

This review is considered an update to AMNT's 2019 review into fund managers' voting policies and practices.

[1] https://www.fca.org.uk/news/speeches/partnerships-priorities-predictions-pensions

KEY REGULATORY DEVELOPMENTS

Climate change is arguably the most important ESG risk facing humanity, investors included. The UN Secretary-General, Antonio Guterres, described the latest report[2] on climate change from the Intergovernmental Panel on Climate Change (IPCC) as "a code red for humanity". According to him: "The alarm bells are deafening, and the evidence is irrefutable: greenhouse gas emissions from fossil fuel burning and deforestation are choking our planet and putting billions of people at immediate risk." **The commitment to achieve global warming well below 2 degrees – ideally 1.5 degrees (or net zero emissions[3]) by 2050 could not be more urgent.**

Recently, the broad UK policy signal has become even stronger on climate change. As part of its November 2020 Ten Point Plan for a Green Industrial Revolution, the UK government stated its desire to position the UK as a leader in the global voluntary carbon market and to drive better data on the environmental impact of companies, supporting investors, businesses and consumers to make green financial decisions and accelerating the transition to a net zero economy as defined above.

Given their crucial role in achieving the Ten Point Plan, investors have also been the focus for the UK government with regard to climate change. The FCA are consulting on new climate change disclosure rules for asset managers in alignment with the Task Force on Climate-related Financial Disclosures (TCFD) recommendations. The Department for Work and Pensions' (DWP) climate change governance and reporting regulations requires trustees of larger schemes to have effective arrangements for the assessment and management of climate risks and opportunities from October 2021, and to report on these in line with the TCFD's recommendations. Put simply, this means that both fund managers and asset owners will need to publicly disclose how they are tackling climate change in their portfolios. Given that the majority of UK pension schemes are externally managed, this means that fund managers need to be clear and robust to their asset owner clients as to how they are tackling climate change across all aspects of their investment decision making, including how they vote and engage with the companies in which they invest on their clients' behalf.

This is why our study is focussed on fund managers, as it reflects the current governance arrangements of the majority of UK pension schemes. In the same Business Plan, the FCA has also recognised the importance of stewardship including voting by stating that they will monitor the exercise of investor stewardship by institutional investors, including voting at Annual General Meetings. "If there is insufficient evidence of active stewardship to advance environmental and social goals, we will consider further regulatory action"[4].

Two take-away messages are apparent from the UK government's climate change commitment: its desire to be a leader in the financial sector, and to drive transparency and accountability to support better investment decision making with regards to achieving net zero commitments.

[2] Climate change widespread, rapid, and intensifying – IPCC — IPCC
[3] Net zero emissions are achieved when anthropogenic emissions of greenhouse gases to the atmosphere are balanced by anthropogenic removals over a specified period.
[4] Business Plan 2021/22 (fca.org.uk)

THE IMPORTANCE OF CLEAR AND ROBUST VOTING POLICIES AND GUIDELINES

A typical pension scheme has multiple fund managers investing in large numbers of companies on their behalf, due to their propensity for passive investment. Given the resourcing of fund manager stewardship teams, it is not practical for the responsible investment teams of their external fund managers to engage with all these companies on environmental, social and governance (ESG) issues. As a result, for most of the portfolio companies, voting is the only communication tool between them and their ultimate investor (the pension scheme), thus magnifying its importance especially in relation to climate change. This means the external fund managers of pension schemes need to implement clear and robust voting policies[5] and guidelines on climate change in order to send a clear and strong signal to companies that they need to transition their business models to well below 2 degrees. As most fund managers continue to refuse to accept client voting policies in pooled funds, then if the fund managers themselves do not have clear and robust guidelines, asset owners cannot meet their own commitments to be well below 2 degrees.

Given the fund manager feedback AMNT has received during our previous review, an important question remains: why is this study focused on voting policies and not on how the fund manager actually voted (voting outcomes)? Other studies have focussed on voting outcomes which AMNT does not argue is an important piece of the "stewardship puzzle". [6]However, when a pension scheme is evaluating a fund manager's approach to voting on climate change, looking at only the voting outcomes is like evaluating the issue with one eye closed.

A pension scheme should be able to ascertain what their fund managers expect of investee companies when it comes to climate change in advance, not just after they have already voted. It should also be able to determine how the fund manager will vote when that expectation is not met (voting guideline). This voting guideline could be triggered automatically when the expectation is not met, or after failed engagement. Either way, the fund manager should be clear about what they intend their vote of dissent to be. There is also the equally important issue of efficiency: a pension scheme should not have to sift through hundreds of pages of voting records and stewardship reports of multiple managers in order to analyse how robust their fund manager's approach has been, when they can simply use the voting policy and guideline as their assurance of the same, and then checking the stewardship reports to confirm that the fund manager has followed their own public commitment. It is also more efficient if all the information pertaining to climate change and voting is in one primary document (hyperlinks acceptable) – this issue is explored further in Methodology.

Because fund managers continue to refuse to accept trustees' voting policies in pooled funds, accessibility of fund manager voting policies and guidelines are a crucial part of a pension scheme's fund manager selection, appointment and monitoring processes. Without that transparency, it hinders the ability of pension schemes to make effective investment decisions, and ultimately may hinder their ability to be able to meet their own regulatory obligations on climate.

[5] For the purpose of this review, AMNT has defined a voting policy as the expectation(s) that the fund manager has for an investee company regarding the ESG issue in question. It may also explicitly include the investment belief that the fund manager has.
[6] Voting-Matters-2020.pdf (shareaction.org)

2. AMNT Review

2.1 AMNT RED LINES POLICIES AND GUIDELINES ON CLIMATE CHANGE

In June 2021[8], AMNT updated its Red Line Voting policies for climate change in several key areas and these form the basis of the 2021 survey. The new policies and guidelines cover five key areas as follows:

Board level responsibility for climate change

If the company does not have a sustainability committee with responsibility for environmental issues including climate change chaired by a board director, or if the company is outside the FTSE 350 and does not have a named board member with responsibility for this area as evidence of appropriate concern, vote against the chair of the board.

TCFD

If the company does not report in line with the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) vote against the chair of the board.

Paris-aligned strategy and science-based targets

Year one: If the company has failed to commit to introduce and disclose science-based emission reduction targets, a coherent strategy and action plan in line with a well-below 2 degrees (ideally 1.5 degrees scenario), vote against the chair of the board.

Year two: if the company has failed to introduce and disclose as above, vote against the chair of the board.

Note that for the purpose of this study, the Paris-aligned strategy and science-based targets have been split into two different categories when evaluating the fund managers' voting policies and guidelines.

Remuneration

Vote against the remuneration policy if the CEO's remuneration package does not include criteria for awards to be linked to relevant sustainability targets including those in relation to climate change

Climate change lobbying

If the company has not stated that it will conduct all its lobbying in line with the goals of the Paris Agreement and does not list its climate-related lobbying activities, vote against the chair.

The fund managers' policies were compared with these Red Lines – the specific requirements under each of these Red Lines are discussed further in the next section.

2.2 TERMINOLOGY

As there appears to be no standardisation as to how voting policies and guidelines are defined, for the purposes of this report we define the terms below as follows:

A **voting policy** can be defined as a description of the expectation that the fund manager has for an investee company regarding the ESG issue in question. It may also explicitly include the investment belief that the fund manager has. For cross referencing purposes, other terminology that investors use include: voting principles and company expectations. An example of a good voting policy is below:

We expect companies to begin reporting climate governance, strategy, policies and performance against the Taskforce disclosure framework[9]

Note that some fund managers having voting policies and guidelines, voting policies only or voting guidelines only. For those fund managers who only have voting guidelines (refer to definition below), credit will be given for having a voting policy if the

[8] AMNT updates 'Red Lines' to reflect the introduction of new policies on climate change, gender diversity, human rights risks and audit - The Association of Member Nominated Trustees
[9] Aviva 2021 Voting Policy

voting guidelines are described in such a way that the specific requirements stated in the review methodology and Appendix A are met.

A **voting guideline** can be defined as a voting instruction that a fund manager will or may take subject to, for example, engagement outcomes. We consider it implicit that any fund manager that has a voting guideline will also have a voting principle even if the latter is not explicit in their voting policy. An example of a good voting guideline, which connects to the above example of a voting principle, is below:

We will consider recommending voting against the chair of the board or other responsible directors of companies which we do not believe to have demonstrated sufficient management of climate-related risks, for example, those UK companies scoring below a Level 4 management rating from TPI.[10]

2.3 REVIEW METHODOLOGY

Where accessible, the most updated UK public voting policies and guidelines (as of April 2021) on climate change of the following 30 fund managers were reviewed.

AberdeenStandard Investments
AVIVA
AXA
BAILLIE GIFFORD
BARINGS
BlackRock
COLUMBIA THREADNEEDLE INVESTMENTS
Dimensional DIMENSIONAL FUND ADVISORS LTD.
Fidelity INTERNATIONAL
Goldman Sachs
Federated Hermes*
HSBC
Invesco
Janus Henderson INVESTORS
J.P.Morgan
Kempen
LGIM
M&G
MFS
Morgan Stanley
NEWTON Investment Management
Pru part of M&G plc
RBC Royal Bank
ROYAL LONDON ASSET MANAGEMENT
Russell Investments
Schroders
STATE STREET
UBS
Vanguard
WELLINGTON MANAGEMENT

[10] Federated Hermes - EOS UK Voting Policy

*Federated Hermes use EOS as their overlay provider and thus their UK voting policy was also reviewed

In view of the very substantial influence of the two global proxy voting companies ISS and Glass Lewis that provide their clients with voting recommendations, we included them in our study. Many fund managers and investors use the services of these two companies. Some will have the proxy voting companies recommend voting actions in accordance with the fund manager's own policy; others may use ISS and Glass Lewis's own voting policy. In either case they could receive the proxy voting company's recommendations on how to vote on AGM resolutions and accept or reject that advice. A recent study[11] indicated that an ISS recommendation can have a 10-15% impact on UK voting outcomes. It is important therefore to include their own voting policies in this study.

As previously stated, the fund managers were compared against AMNT's Red Lines under the following categories:

- TCFD
- Board level responsibility
- Paris-aligned strategy to address climate change
- Science-based targets
- Remuneration targets dedicated to climate change
- Lobbying activities on climate change

Appendix A provides further detail on the methodology used. However certain themes arose from our review that deserve special mention here.

Given the urgency to bring global warming down to well below 2 degrees (ideally 1.5 degrees), the language that fund managers use to describe what they expect of investee companies on climate is absolutely crucial. Put simply, 2021 requires a degree of specificity and robustness unlike ever before, that shows a demonstrable link to policy signalling on climate change (like AMNT's Red Lines). Vague language can no longer be tolerated. Therefore, the use of language was key in our assessment as to whether their voting policies were considered to be aligned with AMNT's Red Lines, and indeed with policy signalling on climate change. For example:

- Specific reference to strategies being Paris-aligned (or net zero, or 1.5 degrees/well below 2) as opposed to just a strategy to address climate change, or only focussing on emissions reduction.
- Specific reference to targets being science-based, Paris-aligned, or net zero, as opposed to using terminology such as "emissions reduction", or merely "targets"

AMNT contacted the 30 fund managers to confirm the accuracy of the information that it was using to inform its analysis. Many fund managers provided AMNT other climate change-related documents – some referred to as their "approach to climate change" or as "insights" for example. Unless these documents were hyperlinked in their primary voting policy document (e.g. LGIM did this, and were credited accordingly), this information was not counted. This was to ensure fairness and a like for like comparison between fund managers, but also due to the issue of efficiency which was highlighted earlier. Overall, we found the arguments for slicing and dicing policies across multiple documents with a complete lack of any clear cross-referencing wholly unpersuasive. If climate change was an important enough topic to merit a separate document, why is it not important enough to cross-reference it from the main voting policy or indeed update the latter if necessary? Speaking to the efficiency argument earlier, schemes should not have to search for and compile disparate documents across the fund managers' websites in order to ascertain an accurate picture as to what the fund managers' position is on climate related voting. The way voting-related (or indeed any ESG or stewardship) information is presented to pension schemes is just as important as what the information is. This is especially true for documents which appeared to be informational or marketing materials only.

Some fund managers referred AMNT to their voting records and stewardship reporting as evidence of them taking action on climate change. While voting outcomes are an important part of the piece, they are not a replacement for clear and robust voting policies and guidelines that send a clear signal to asset owners, clients and investee companies **prior to the AGM season.** They are also an essential tool for trustees to use to judge the fund managers' actions. Therefore, voting records and stewardship reporting were not given credit for having a voting policy and guideline on climate.

[11] www.pwc.co.uk/services/human-resource-services/insights/demystifying-executive-pay/iss-friend-or-foe-to-stewardship.html

› 3. Findings

Key findings are highlighted below. Note that when referring to percentages (e.g. a third, half etc), the reference will be against the 30 fund managers, which includes the two which did not disclose a voting policy on any ESG issue.

3.1 VOTING POLICY

Of the 30 fund managers reviewed:

> Two fund managers, Barings and PGIM, did not publicly disclose their voting policies on any ESG issue for any market

> Two major passive fund managers, State Street and Vanguard, **do not reference climate change at all in their UK voting policies or guidelines[12].** Vanguard subsequently provided AMNT with supplemental materials on their company expectations on climate change. State Street also has a dedicated section on their website on climate stewardship highlighting their voting outcomes on climate. However as per Section 2.3, neither Vanguard nor State Street were given credit.

  The remaining fund managers in this category are Janus Henderson, JP Morgan, and MFS for a total of five. JP Morgan referenced climate change in their non-US voting policy but not for UK companies.

> Five fund managers' references to climate change in their voting policy did not meet any of AMNT's Red Line climate change policies. These fund managers are: Baillie Gifford, Fidelity, Invesco, M&G, and Russell.

> **Four fund managers** had voting policies and guidelines which met all five of AMNT's policies (Aviva, Blackrock, Federated Hermes and LGIM).

> Neither ISS nor Glass Lewis had voting policies for climate change that met AMNT 's Red Line climate change policies.

In summary, the above findings mean that ***40%*** *of the fund managers (12/30) either*:

> *Do not disclose their voting policy on any ESG issue; or*

> *Do not reference climate change in their voting policy at all; or*

> *Reference climate change but none of their references met AMNT's Red Line voting policies on climate and thus reasonable standards for taking action on climate change. Neither of the dominant proxy advisors - ISS or Glass Lewis - have voting policies for climate change that reflected AMNT's policies, and thus reasonable standards for taking action on climate change.*

The remaining fund managers – those that had some climate change references that met AMNT's policies, are summarised below by category (also refer to Table 2 in Appendix A).

TCFD: A little over half of the fund managers (16) referenced TCFD in their voting policies. Nine of these fund managers only recommended that companies use the framework to disclose what they are doing on climate (versus asking them to have a strategy that is in alignment with TCFD recommendations). As a result and as per the methodology, these nine fund managers did not get credit for board level responsibility, strategy, targets and remuneration.

Board level responsibility on climate change: Twelve fund managers (40%) referenced board level responsibility for climate. Four fund managers were not given credit for this criteria because they only made reference to board level responsibility for environmental and/or social issues, and did not specifically reference climate change.

Paris-aligned strategy: Ten fund managers (a third) made a specific reference to companies needing to have a Paris-aligned or net zero climate strategy (or similar language), and even fewer make specific reference to the need for that strategy to be made public for shareholder review.

[12] Note Vanguard provided separate documents on climate change related work that they are doing with investee companies. For reasons stated in Section 2.3, this information was not counted. State Street did not respond to AMNT's email.

Science based targets: Ten fund managers (a third) referenced science-based, net zero or Paris-aligned targets. Some fund managers only referenced targets or emission reduction in general terms but with no qualifier as to what benchmark the targets would be based on. As such, these fund managers were not given credit for all the reasons stated in Section 2.3 regarding the use of robust language.

Remuneration: Nine fund managers (a little less than a third) referenced remuneration targets on climate change. Similar to board level responsibility, credit was not given to those managers who referenced remuneration targets for environmental issues but do not specify climate change specifically.

Climate change lobbying: This was the poorest performing category, with only six fund managers (a little over 20%) referencing climate change lobbying. The majority of those were focussed on disclosure of their lobbying activities on climate, versus asking companies to take specific action on climate in their lobbying approach.

Overall the number of fund managers that met AMNT's individual policies on climate change was quite low (a little over half for TCFD and for the remaining categories 40% or less), and thus do not have reasonable standards for taking action on climate change.

3.2 VOTING GUIDELINES

> Nine fund managers (almost a third) have no voting guideline at all. Six of those do not have a voting guideline because they do not have a voting policy on climate. They are: Dimensional, Janus Henderson, JP Morgan, MFS, State Street and Vanguard. The remaining fund managers met some of AMNT's policies on climate but did not have a voting guideline. They are: Aberdeen Standard, Baillie Gifford, and Newton.

> Eighteen fund managers having a voting guideline on climate change. Of those 18:

- Seven fund managers have a voting guideline which only references their potential support for climate change shareholder resolutions (including in some cases the weak term "evaluate on a case by case" basis). They are: Invesco, Kempen, Russell, RBC, Russell, UBS and Wellington.

- Only eight fund managers would target directors who do not meet certain expectations on climate change. They are: Blackrock, Federated Hermes, HSBC, LGIM, RBC, RLAM, Schroders and UBS. Of those, just over half of those (5) explicitly referenced the Chair (Federated Hermes, HSBC, LGIM, RLAM and UBS).

> The climate change expectation which triggers voting action was generally unclear, with a couple of exceptions (LGIM, Federated Hermes). Stating that they will use their vote of dissent for "insufficient disclosure" or "insufficient risk oversight" is not specific enough to determine what will actually trigger the vote of dissent

> ISS has the following voting guideline which, similar to above, is unclear as to what specific action will trigger a vote of dissent on climate change[13]:

ISS: Under extraordinary circumstances, ISS will consider recommending a vote against individual directors for: Material failures of governance, stewardship, or risk oversight (including, but not limited to, environmental, social, and climate change issues)

> Glass Lewis referenced supporting shareholder resolutions on climate-related disclosure and lobbying on a case by case basis, subject to certain criteria.

In summary, only eight fund managers of 30 reviewed would target directors for insufficient disclosure or action taken on climate change. Of those eight, only five of them would target the Chair. Of the 18 that had a voting guideline, nearly 40% of them only had a voting guideline for shareholder resolutions.

[13] ISS is currently reviewing its voting policy on climate and has put out a public consultation: ISS Opens Global Annual Benchmark Policy Survey and Separate Climate Survey (issgovernance.com)

› 4. Discussion of findings

The key findings under voting policy and voting guideline are briefly highlighted below followed by a discussion.

VOTING POLICY KEY FINDINGS:

1. ***40%*** *of the fund managers (12/30) either:*

> *Did not disclose their voting policy on any ESG issue; or*

> *Did not reference climate change in their voting policy at all; or*

> *Referenced climate change but none of their references met AMNT's Red Line voting policies on climate and thus reasonable standards for taking action on climate change.*

2. *Of the remaining fund managers, the number of fund managers that met AMNT's individual policies on climate change was quite low (a little over half for TCFD and for the remaining categories 40% or less), and thus in our view do not constitute reasonable standards for taking action on climate change.*

3. *Neither of the dominant proxy advisors - ISS or Glass Lewis - have voting policies and guidelines for climate change that reflected AMNT's policies, and thus reasonable standards for taking action on climate change*

This is a surprising find given the market and regulatory framework in which the UK is currently operating, **especially if the UK government wishes to be a global leader on green finance.** The four fund managers that either met or came close to meeting AMNT's policies on climate change demonstrate that there is no sufficient reason why the remaining fund managers are not at the same level. As indicated in the analysis of the individual AMNT policies above, it is clear that language and terminology are playing an important role here and must be addressed. Not explicitly referencing climate in board level responsibility, or only stating "emissions reduction" is simply not sufficient in a post-Paris Agreement world, neither is the lack of references to Paris aligned strategies and climate-linked remuneration. The question remains as to whether this indicates a lack of buy-in on the stewardship side of the fund management industry regarding climate change (versus its product development department for example) or whether this is a case of fund manager unwillingness to be more transparent about their stewardship approach to allow for greater flexibility.

Of particular note is State Street and Vanguard, considering the dominance they have in UK's passive equities market. State Street has a global environmental and social voting policy, but it does not contain any information on what it expects of companies vis a vis climate change, nor a voting guideline. Vanguard makes reference to environmental issues in its policy, but not climate change. To fail to explicitly reference climate change, and instead use the term "environmental", is simply not sufficient for 2021. Based on a cursory review of their respective voting records, stewardship reports and supplemental materials[14], it is clear that both State Street and Vanguard do take action on climate change for select investee companies as part of their stewardship approach, as likely do other fund managers forming part of this study who did not meet AMNT's policies. However, demonstrating voting outcomes on climate change without being able to relate those outcomes to a voting policy, OR having disparate documents with no apparent connection to the voting policy, weakens the fund manager's stance on the issue. It also hinders trustees' ability to be able to hold fund managers to account for their stewardship approach, because they do not have a voting policy as a benchmark against which to judge the fund managers' performance (unless the trustee has their own). It gives too much freedom for the fund manager to act on a case by case basis, which sends a weaker signal to investee companies. If we want the entire investment chain – including companies – to have a Paris-aligned approach to addressing climate change, then consistent signalling at policy level is absolutely vital. Strong policies and outcomes are the way forward, not just the outcomes. With respect to supplementary materials such as that provided to us by Vanguard, it is very important that any relevant information such as company expectations or voting guidelines be put into the formal voting policy. By doing this, it gives the issue greater legitimacy to stakeholders.

[14] Vanguard example: ISCLRG_062020.pdf (vanguard.com)

VOTING GUIDELINE KEY FINDINGS:

> *Only eight of the 30 fund managers reviewed would target directors for insufficient disclosure or action taken on climate change.*

> *Of those eight, only five of them would target the Chair.*

> *Of the 18 that had a voting guideline, nearly 40% of them only had a voting guideline for shareholder resolutions.*

> *Glass Lewis's voting guidelines only referenced shareholder resolutions, and ISS made a cursory reference using weak language ("exceptional circumstances").*

Very few fund managers of those reviewed – roughly 25% - would target directors if insufficient disclosure or action was taken on climate change. Given that climate change is considered by policy makers and regulatory bodies as a material financial risk and thus directors should be accountable for its management, this is a disappointing finding. Compounding the issue is the significant percentage of fund managers that have a voting guideline, but only for shareholder resolutions. This is a significant concern because, for a financially material risk like climate change, if there are no shareholder resolutions put forth at a company, the fund manager has no policy or guideline on the issue and is not holding companies to account at all. This is particularly material for the UK market, in which shareholder resolutions are rarely proposed. Glass Lewis, which covers more than 30,000 shareholder meetings, has reported that the total number of shareholder proposals they reviewed in 2020 was 434, of which just 17 concerned climate change.[15]

When the lack of or poor disclosure on voting guidelines was discussed with fund managers during AMNT's initial analysis two years ago, the main feedback received was that they wished to maintain flexibility in their voting actions. Given that some fund managers are very clear and robust on how they will vote if their expectations are not met (e.g. LGIM, Federated Hermes), we see no reason why the other fund managers should be using the flexibility argument in 2021. As stated in AMNT's 2019 report, trustees require this level of transparency so that they can effectively hold their fund managers to account. If they don't know what their fund managers' voting intentions are, how can they scrutinize their approach, or indeed if necessary, request vote deviations in alignment with their own position on the issue? This also compels the fund manager to be more publicly accountable (or at least to their clients privately) about when they have deviated from that voting guideline, which AMNT considers is very important.

Even for those fund managers who do have a voting guideline, there are still residual issues remaining regarding the use of language. The first concerns the terms used to describe their voting action regarding directors. A significant percentage of the fund managers use terms like "may withhold support", "we will consider voting against", "we may take voting action to highlight this", or "we will generally vote against". However, there are some that take a more robust stance such as Aviva ("we will not support") and LGIM ("we have already publicly committed to voting against the chair of the board"). This suggests that the flexibility argument does not hold true for every fund manager, and therefore it is possible to take a more robust stance on the issue, but the majority of fund managers choose not to.

This may seem a pedantic analysis at first glance, but given that these policies are reviewed by compliance departments prior to publication, we do not believe the choice of language is an accident. Fund managers are not generally willing to publicly state what they will actually do – not may or could – if expectations are not met. Overall, we have concerns about this type of language being used deliberately to allow greater flexibility for the fund managers.

The second issue concerns the lack of clarity over what may actually trigger the voting sanction. Terms like "insufficient disclosure or risk oversight" does not give sufficient information to determine the threshold that will trigger a vote of dissent. Fund managers should be held to account for both of these issues as it weakens the ability to scrutinise their approach. To be clear, AMNT supports the comply or explain principle when it comes to voting and engagement, and there are good reasons why a fund manager may choose not to take voting action against a company. But there is no reason why a fund manager cannot state what its default voting intention is if certain expectations are not met, and then provide an explanation through appropriate client reporting as to when they have deviated from that position and for what reason. This is the position we advocate.

Whilst we recognise that the fund manager has the ultimate responsibility for the contractual relationship between themselves and their proxy provider, the lack of any reference to climate change in the case of Glass Lewis and the poor reference to it in the case of ISS in our view indicates a failure to recognise the gravity of the climate change crisis, particularly since fund managers (or indeed asset owners) lacking in responsible investment expertise and/or resources may choose to adopt their proxy agency's policy rather than develop their own.

[15] https://www.glasslewis.com/wp-content/uploads/2020/09/2020-Proxy-Season-Review-Shareholder-Proposals.pdf

5. Conclusions and Recommendations

5.1 CONCLUSIONS

Given how high climate change is on the regulatory agenda in the UK, it is very surprising that only four fund managers had a voting policy and guideline that met AMNT's criteria. **It is clear that this issue requires urgent action, especially by the FCA as it relates to not only poor disclosure hindering market competition and the ability of trustees to make effective investment decisions, but also whether fund managers are doing what is necessary to tackle climate change in their approach to voting.**

Lack of robust voting policies and guidelines

Given market and regulatory developments since the Paris Agreement, AMNT expects fund managers to have:

- A voting policy on TCFD requirements, board level responsibility for climate change, Paris-aligned transition strategies, science-based targets, climate-linked remuneration, and climate lobbying.

- A voting guideline targeting directors (in addition to shareholder resolutions etc) for when the voting policy position is not met.

What reasonable conclusion is a trustee supposed to reach if so few fund managers are able to meet this criteria? Does this mean that fund managers don't take climate change, or perhaps environmental and social issues more broadly, seriously? Do they not take the voting function seriously and are more interested in providing climate change-related products to their clients than robust stewardship? Do the fund managers have robust climate change policies internally but do not wish for them to be made public to their clients or more widely (see next section on transparency and accountability)? Do they wish to retain full control over how and what they do and do not wish that information to be in the public domain?

Wherever the problems lie, time is running out for these issues to be addressed when it relates to the policy goals of being well below 2 degrees and achieving net zero carbon emissions by 2050. Lack of transparency by fund managers on climate related voting hinders pension schemes from meeting their own climate-related obligations. The whole voting chain, from investee companies to pension schemes – need to reach this level of transparency and accountability. Otherwise it weakens our policy efforts to achieve net zero by 2050. It only takes one investment actor to weaken the whole chain.

For those trustees who have identified climate change as financially material to their scheme, and wish to have their assets voted in a more robust way, where are they supposed to take their business given these findings? This issue is further exacerbated by the continued refusal of fund managers to accept client voting policies in pooled fund arrangements. Both our previous study, and this study, demonstrates that the trustees' Red Line policies on climate change are more effective than those of most fund managers, but currently most fund managers are insisting that trustees accept their inferior policies. It is for this reason that AMNT submitted their complaint to the Financial Conduct Authority in 2019.

Lack of transparency and accountability – is flexibility a reasonable argument?

AMNT has also been told in the past that the lack of public transparency on these issues is due to the need for flexibility in their stewardship approach, which could stem from anything from the size of the company, sector-based approaches, to allowances for engagement escalation amongst considerations. This likely also explains the use of weak and vague language. In our view, fund managers are allowing too much flexibility in applying their principles should they indeed have any, to such an extent that it hinders accountability. As previously stated, it also begs the question as to why the fund manager wishes to be so opaque in their approach: it casts doubt in the mind of the asset owner client as to how seriously they take the issue if they are not prepared to state what they may do to register dissent to a company. We support some degree of flexibility in stewardship (indeed we welcome it in some cases) but this is so much as to be a hindrance to client trust and market competition. This level of transparency is also important for investee companies so that they have a clear understanding of investors' expectations of them. Investee companies have in the past charged investors with weak or inconsistent signalling across issues of concern, therefore increased transparency and accountability in the voting policy would address this.

It is crucial that fund managers are fully transparent on their voting policy and guideline on climate change so that investee companies and trustees know what to reasonably expect in advance of the Annual General Meeting, barring exceptional circumstances. A trustee should not be left in the dark as to how their fund manager intends to vote, especially if trustees are expected to hold their fund managers to account through benchmarking their own stewardship policies against that of their fund managers.

Voting policies versus outcomes

Another argument put forward by the fund management community is that they can demonstrate proof of their commitment to addressing climate change through their voting records and stewardship reporting. Whilst a review of voting records and stewardship records was beyond the scope of this review, AMNT does not necessarily dispute their commitment through these mechanisms. However, as highlighted in the Introduction, demonstrating outcomes without disclosing your policy position on the issue, gives no context to the outcomes that trustees – or advisors on their behalf – are reviewing. It also calls into question – rightly or wrongly – the commitment of the fund manager on the issue in question. An ad-hoc, case by case approach to addressing climate change is not an adequate policy stance for 2021.

Voting policies versus separate marketing materials on climate

Some fund managers provided AMNT with a lot of information on their approach to climate, how they engage with companies on climate in separate documentation. None of this information however was contained within their voting policies. Trustees should not have to sift through the ESG/stewardship section of their fund managers' websites looking for information on their climate change approach. All voting policy and guideline-related information should be contained in one policy document. Disparate policies create doubt as to how serious the fund manager is taking the issue. Put simply, why isn't it in the policy? If their approach to climate change has evolved since the last update of their voting policy document, why is the policy document itself not updated to reflect this given how serious climate change is as an ESG issue?

5.2 RECOMMENDATIONS

Based on the findings, AMNT has the following recommendations:

Trustees

Trustees should work with their advisors to develop their own voting policy and guideline on ESG issues of material concern to their scheme. If climate change has been identified as one of their priority areas (and we would highly recommend its inclusion), we recommend that they adopt AMNT's RLV policies on climate change. (Those of Aviva, BlackRock, LGIM and Federated Hermes are also good.) Trustees should request that their fund managers adopt these policies. If they refuse to do so the trustees should use the policies and the findings of this report to hold their fund manager to account if their voting policy and guideline does not align with their own policy. Collective pressure from trustees on these key issues is key to achieving real change in this area.

Fund managers

The fund management community should revaluate their voting policy and guidelines in advance of the 2022 proxy voting season and consider whether they are sufficiently clear and robust when compared to AMNT's Red Line climate change policies, and if not, make appropriate revisions to their policies accordingly. Specific recommendations are as follows:

1. Investors should not have to use voting outcomes and stewardship reporting to deduce a fund manager's stance on how they tackle climate change in their voting approach. Public disclosure of voting policies are equally important for complete accountability.

2. Expect investee companies to have climate change governance, strategy, and targets in alignment with TCFD recommendations, rather than merely just asking companies to disclose against TCFD

3. Expect investee companies to publicly disclose their Paris-aligned strategy and science-based/net zero targets

4. Tighten up the use of language with regard to emission reductions – state that the targets must be science-based or net zero.

5. Specify climate when referring to remuneration targets and lobbying activities

6. Target company resolutions – ideally directors – to register a vote of dissent on climate rather than limiting voting action to shareholder resolutions on climate change

7. Be clear as to whom and under what specific circumstances the vote of dissent will be registered – avoid the use of “case by case” by clearly stating under what circumstances shareholder resolutions will be supported.

8. Ensure any additional material released on climate change is hyperlinked in the main voting policy document, where relevant.

Proxy voting agencies

Given their importance in the stewardship chain, we urge ISS and Glass Lewis to introduce explicit climate change voting policies and guidelines in alignment with AMNT’s criteria.

Financial Conduct Authority

In its recent business plan[16], the FCA stated that they “will monitor the exercise of investor stewardship by institutional investors, including voting at Annual General Meetings. If there is insufficient evidence of active stewardship to advance environmental and social goals, we will consider further regulatory action”. They also stated that one of the outcomes they wish to achieve is “high-quality climate- and sustainability-related disclosures to support accurate market pricing, helping consumers choose sustainable investments and drive fair value”. AMNT’s findings indicate there is poor disclosure of voting policies and guidelines on climate change, which will not only hinder consumer choice and investment decision making but, most importantly, calls into question how serious fund managers are about tackling climate change.

Given their own priorities regarding addressing “insufficient evidence of active stewardship in advancing environmental and social goals”, the FCA’s competition arm seek regulatory action to remedy this market failure. This action would serve two important purposes:

> Allow trustees to have the necessary information to make appointment and retention decisions over the asset managers who will implement voting policies that reflect their priorities, and

> Ensure a more robust approach by the fund management community in tackling climate change in their voting approach

Looking ahead – the next frontier

There are two major areas that investors should look to update their voting policies on climate. They are:

Climate accounting

With regard to annual reports, the main focus of investor analysis has been on the “front end” of the report, and not the profit and loss accounts at the “back end”. It is just as important that the calculations and assumption made in determining the financial health of the company take into account climate change. If the calculations and assumptions are incorrect and do not take into account climate change risks, this has a negative impact on capital allocation decisions, the share price of the

[16] Business Plan 2021/22 | FCA

company, what dividends shareholders receive, and so on. To date, based on AMNT's cursory review of this issue in fund manager voting policies, climate accounting has been largely ignored barring a few exceptions. For example, Blackrock and Federated Hermes make reference to the audit function with their climate change section.

Financial reporting should reflect assumptions made about the impact of climate risk and the transition to a low carbon economy on the company's profits, liabilities and assets. (Blackrock)

Companies should ensure that the financial risks associated with climate change and the energy transition are appropriately reflected in reports and accounts. The audit committee should be responsible for ensuring these risks are accounted for. (Federated Hermes).

We urge fund managers to update their voting policies to incorporate climate accounting accordingly, similar to the examples provided.

Testing corporate transition plans – from disclosure to action

The 2021 Shell AGM showcased the future need for investors to develop the necessary tools and expertise to evaluate company transition plans to determine if they are fit for purpose. The Climate Action 100 net zero benchmark, which is used to assess companies' progress towards net zero, is a comprehensive first assessment, however it does not provide investors with more detailed insights into the quality of the individual transition plans of companies. Over time as the market develops in this area, investors need to consider introducing more robust voting action if, after sufficient testing, the corporate transition plans are not Paris-aligned. It is one thing for a company to disclose against the Climate Action 100 benchmark and investors to give them the benefit of the doubt that these disclosures are aligned with the Paris Accord. But it is quite another to test their facts and figures and have that analysis drive voting action. The latter action is crucial and as previously stated, requires a gap in tools and expertise to be filled as soon as possible.

Appendix A

RESEARCH METHODOLOGY

We broadly divided the fund managers into the following categories:

1. No public disclosure of their entire policy document

2. No public disclosure of their voting policy and guideline on climate change (i.e., does not reference climate change at all in their policy document)

3. Public disclosure of their voting policy on climate change divided into the following categories[17]:

> Board level responsibility for climate change - this can fall under sustainability issues but climate change must be explicitly referenced. An expectation of a group-level policy was given credit as board-level responsibility is implicit.

> Reference to TCFD – the use of language is an important consideration for this particular policy. Any company expectation regarding TCFD will be given credit; however the nature of the expectation will determine whether credit is given for other areas if the other areas are not explicitly referenced as well. For example, only asking a company to "report against" TCFD will not automatically give the fund manager credit for board-level responsibility, strategy, targets and remuneration, unless they are explicitly referenced as well. This is due to the comply or explain aspect of the TCFD requirement, meaning that a company could technically respond that they don't have these mechanisms in place.

However, if the fund manager expects that companies have climate change governance structure and strategy in alignment with TCFD recommendations, that is different and will be given credit for the other areas (board-level responsibility, strategy, targets and remuneration). Note that TCFD does not explicitly reference an expectation regarding climate change lobbying as of the date of this report.

> Paris-aligned strategy to address climate change – fund managers will not be penalised if they expect companies to have this strategy but don't require public disclosure, however we note any differences in approach within the discussion section. Partial disclosures in this area will be not given credit (e.g. requiring companies to disclose and explain their capital expenditures, or scenario testing). Fund managers having an overall internal commitment to net zero does not count unless they further describe what they expect of investee companies. This is because we cannot assume that their internal net zero strategy includes the same commitment for their investee companies unless they explicitly state it.

> Science-based (or net zero) targets: reference to a reduction in emissions, or target setting without specifying that the targets should be Paris aligned, net zero, or science-based were not counted. However, we did note differences between policies in the discussion section.

> Climate change targets within their executive remuneration – as for board level responsibility, targets can be referred to as sustainability-related but climate change needs to be explicitly referenced as per board level responsibility.

> Climate change lobbying – reference to better disclosure and accountability with respect to companies and their lobbying activities re climate change will be given credit.

4. No public disclosure of their voting guideline on climate change.

[17] Categories were chosen based on RLV policies on climate change

5. Public disclosure of their voting guideline on climate change divided into the following issues:

> Company versus shareholder resolutions. In the case of company resolutions, we note which resolution is targeted (e.g. Chair, directors, report and accounts etc). In the case of shareholder resolutions, we have given credit to shareholder resolutions of climate change where the fund manager uses a “case by case” approach to evaluating whether or not they will support it. However, these types of resolutions have been distinguished from the rest for the purpose of further discussion. Some fund managers referenced support for shareholder resolutions for a topic covered under the voting policy (e.g. TCFD). As long as the content of the voting guidelines met the requirement of the voting policy as described above, it was given credit.

> Climate change theme of the resolution (e.g. disclosure)

This study was of UK voting policies, not those of other markets. If the fund manager referenced climate change in other regional voting policies but not their UK one, they were not given credit. If the fund manager only had a global voting policy, then the UK market was considered to be included in that. If the fund manager provided hyperlinks in the voting policies to other relevant documents which aid to supplement their policy position on climate change (e.g. dedicated climate change policy or climate company scorecard), credit was given.

Supplementary materials on climate change

Some fund managers may choose to supplement their voting policies with additional marketing materials (e.g. newsletters etc) on ESG themes like climate change. They may even contain investee company expectations, questions they will ask company boards on climate etc. While these materials may be useful to clients, if this information is not contained, referred to or with links provided, within the voting policy itself, it has not been counted.

The use of language and participation in collaborative initiatives

The significance of language in fund manager voting policies should not be underestimated. Some fund managers use weak language such as “we encourage” or “companies should consider” while others use stronger language such as “we expect” or “companies should do X”. While we will give credit for the policy even if weak language is used, we have distinguished them from the stronger language for the purpose of further discussion. A similar approach was used for voting guidelines. Some fund managers use weak language such as “we may choose to vote…” or “we will consider voting against”. versus some that say that they **will register** a vote of dissent if the company does not meet the voting policy expectations.

AMNT recognises the importance of investor collaborations like Climate Action 100+ and its net zero benchmark[18], and the Transition Pathway Initiative[19](TPI). These initiatives do cover some if not all of the policies analysed as part of this study. However, sole reference to being part of an investor collaboration such as Climate Action 100+ or TPI with no further information provided will not be counted as having a voting policy on climate change under the above categories. It is important that investors are explicit in their policy about what they expect of investee companies, and not just simply reference collaborative initiatives.

Climate change outcomes and reporting

The focus of AMNT’s review was on fund manager voting policies and guidelines, not voting records or stewardship reporting. Therefore, if a fund manager makes no reference to climate change in their voting policy document, but references climate change in their voting records or other stewardship reporting, credit was not given.

[18] Framework and Methodologies | Climate Action 100+
[19] Home - Transition Pathway Initiative

Table 2 - Breakdown of each individual category

AMNT criteria	Number of fund managers who met AMNT criteria	Good practice example
TCFD	16/30	We expect companies to begin reporting climate governance, strategy, policies and performance against the Taskforce disclosure framework *Aviva*
Board level responsibility	12/30	We urge companies not already doing so to: Establish strong governance of the risks and opportunities presented by climate change. Boards should ensure that climate change is included on the board agenda at least annually. We recommend that the board and senior management engage with outside experts who can advise on strategic risks and opportunities that climate change presents, including challenging the company's approach if necessary. For those companies materially exposed to climate related risks and opportunities, we expect the energy transition to be clearly articulated in governance documents, including board committee charters and the articles of association. *Federated Hermes (EOS)*
Strategy	10/30	We expect all companies to clearly articulate climate strategies and transition pathways that will deliver net zero emissions by the middle of the century. *Aviva*
Science-based targets (net zero)	10/30	We expect companies to articulate how they are aligned to a scenario in which global warming is limited to well below 2°C and which is consistent with a global aspiration to reach net zero Greenhouse Gas (GHG) emissions by 2050. *Blackrock* We encourage companies to commit to the Science Based Targets Initiative (SBTi) framework. Climate strategies should include near and medium-term targets and provide investors an understanding of how capital allocation will be adjusted over time to support the transition of the business. *Aviva*

AMNT criteria	Number of fund managers who met AMNT criteria	Good practice example
Remuneration	9/30	We would expect short and long-term variable pay to include robust and relevant sustainability metrics that have a meaningful impact on total pay outcomes. This should include climate related objectives for high carbon emitting sectors. *Aviva*
Lobbying	6/30	We also expect boards to review all trade association funding and political lobbying activities and ensure it is fully aligned with the company's public position and policies on climate change. *Aviva* Ultimately the board should be prepared to cease membership where misalignment persists without progress. *Federated Hermes (EOS)*

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