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ABOUT THIS REPORT
The 2020 Governance Outlook: Projections on Emerging Board Matters is designed to give corporate directors and senior executives a comprehensive overview of major business and governance issues likely to demand board focus over the coming year. The report begins with an introduction from NACD, highlighting survey findings about leading board priorities for 2020, and follows with eight partner contributions that provide distinct insights and projections on the following themes: preparing for the next recession, strategic business risks, regulatory changes, legal risks, board composition, the digital frontier, ESG and engagement, and water scarcity risk.

Each partner contribution provides (1) an overview of key trends in a particular area of governance, (2) an outlook for how those trends will play out in 2019, and (3) relevant implications and questions for boards to consider. The 2020 Governance Outlook: Projections on Emerging Board Matters is designed as a collection of observations to help corporate boards prioritize their focus in 2020 and increase their awareness of emerging issues, through both detailed topical analysis and coverage of broader governance implications.
Brace Yourself for an Eventful Year
Shareholder engagement is the watchword for 2020, thanks to the nexus of constituents focused on environmental, social, and governance (ESG) issues. Interest in ESG among institutional investors is heating up at a time when employees and smaller shareholders—particularly millennials—are pushing companies to think beyond the bottom line.

Boards that effectively utilize technology to improve external communications are better positioned to both “sense” and address stakeholders’ growing focus on board diversity, climate change, and other ESG issues. This effective utilization ranges from monitoring social media to analyzing proxy-voting outcomes on ESG matters among peer companies. Recent regulatory developments that would place limits on shareholder proposals and proxy advice are not expected to diminish increasing expectations for corporations to demonstrate progress on making a positive impact on society. Management and boards should expect continued engagement with shareholders, not only in annual shareholder meetings but throughout the year.

Participation | Percentage of Shares Voted

Yet, in many cases, directors do not have a complete view of all shareholders’ sentiment. Across all US companies, around 30 percent of shares on average are held by retail investors, but they vote only 28 percent of the shares they own, according to ProxyPulse. Conversely, institutional investors hold about 70 percent of the shares (and vote 90% of them), so their voices are more likely to be heard.¹

Management and directors that communicate business strategies, ESG policies, and significant business developments—through notifications and news feeds to retail investors’ mobile phones—are bringing more small shareholders out of the shadows. Broadridge reports a record 2.7 million retail positions were voted via MobileProxyVote.com during the 2019 proxy season, and more than two million positions were cast from brokerage websites via Investor Mailbox.² Voting is also now possible from some apps.

When they engage, retail shareholders can make a significant impact, because their ownership, as a segment, is on average greater than the very largest institutional investors. Retail investors are typically performance oriented—when they vote, they reward companies that perform well, and when they are unhappy, they often “vote with their feet” by selling their shares. The challenge for boards and managers is to provide easily-digestible communications, on ESG and other topics. “Layered” proxy disclosures that offer summaries of key information in microsites can also reduce the effort to vote.

Key Projections

ESG Will Continue to Be at the Fore
Due to rising expectations for corporations to make a positive impact on society, ESG will continue to be an important aspect of board engagement for shareholders, employees, and proxy advisors focused on long-term business impact.

ESG engagement efforts come at a time of increased pressure generally on directors. The number of directors failing to receive majority support (at least 50% in favor) continues to climb, from 345 in 2015 to 478 in 2019, based on votes processed by Broadridge—despite fewer directors up for election.³

Moreover, the number of directors failing to receive at least 70 percent support has also continued to increase, from 1,185 in 2015 to 1,726 in 2019.⁴ Failure to surpass this threshold can result in recommendations against directors in following years.

⁴ Ibid.
These trends are happening despite generally rising stock valuations. Good performance alone does not guarantee that all constituents will support directors. Heading into 2020, boards need to develop new and robust means of engaging all stakeholders on companies’ ESG policies and progress. “We are in the throes of a historical shift in perception” about the impact of climate change and investors’ desire to express their views on the subject, says Dr. Alexis Crow, PwC’s lead, Geopolitical Investing.5

Globally, sustainable investing assets stood at $30.7 trillion at the start of 2018, a 34 percent increase in two years, according to the Global Sustainable Investment (GSI) Alliance.6 Total US-domiciled assets under

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6 GSI Alliance, 2018 Global Sustainable Investment Review, p. 5.
7 Ibid., p. 6.
management using sustainable strategies and related ESG criteria grew 38 percent to $12 trillion in recent years.\(^7\)

The Paris Climate Accord immediately comes to mind with the term ESG. However, ESG has come to mean much more—covering board diversity, shareholder voting rights, board independence, and other matters. Good governance is a part and parcel of making a positive impact on society.

There are many signs of progress. For example, the number of ESG-related shareholder proposals declined to 381 in 2019 from its peak of 426 in 2015, in part because companies are taking proactive steps and engaging with investors outside of the annual shareholder meeting process. But that’s no reason for complacency, because when ESG proposals come up for a vote, as a result of concerted campaigns or other shareholder action, institutional support has been rising. Over the past four years, it rose from 25 percent in 2015 to 32 percent in 2019. By contrast, retail shareholders were less supportive of such proposals over the same time frame: when they voted, retail support was in the low-to-mid teens.\(^8\)

We expect that could change as millennials surpass 50 percent of the US workforce in 2020, and as growing numbers of them own more stock. Multiple surveys show climate change to be the most important issue to people born between 1981 and 1996.\(^9\) As employees, shareholders, and consumers, millennials are an increasingly important constituency to corporations. Board members, in turn, need to anticipate the concerns and sentiments of this shareholder cohort.

Recent events at Amazon provide a strong indicator of the changes to come, as directors think about the broader stakeholder engagement.

At its 2019 annual meeting, Amazon’s board recommended a vote against a climate-change proposal calling for the company to report how it is “planning for disruptions posed by climate change, and how Amazon is reducing its company-wide dependence on fossil fuels.”\(^10\)

The proposal, put forth by roughly 8,000 employees, received just 30 percent support from shareholders,\(^11\) but the issue remained of paramount importance to Amazon’s workers. In September, as Amazon employees prepared to join a larger protest over the tech industry’s perceived inaction on climate, the company announced that it was the first signatory of

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\(^6\) Based on Broadridge’s 2019 ProxyPulse™ data. It covers the results of 4,059 public company annual meetings held between January 1 and June 30, 2019. ProxyPulse data is based on Broadridge’s processing of shares held in street name. The five-year trend data covers the proxy season, which is when the majority of public company meetings occur.


\(^8\) “Amazon: Adopt the Workers’ Climate Plan Resolution,” posted on ActionNetwork.org.


\(^10\) Amazon, “Amazon Co-Founder’s Climate Pledge, Setting Goal to Meet the Paris Agreement 10 Years Early,” Amazon.com press release, September 19, 2019.
“The Climate Pledge,” and committed to net zero carbon emissions by 2040, a decade ahead of the Paris accord’s goal.\textsuperscript{12}

As the Amazon example suggests, broad groups of stakeholders will likely continue to make ESG demands of management and director “mindshare” in 2020 and immediately beyond. Boards should ensure that their companies have identified the most relevant stakeholder groups and that they have a robust strategy to engage with them. Companies may want to give a higher profile to communications on their progress in ESG areas.

**Proxy Advisory Policies Will Continue to Impact Voting**

Board members will continue to focus on policy recommendations coming from proxy advisory firms. For example, Glass Lewis announced it will “recommend supporting well-crafted, binding shareholder proposals that increase shareholder value or protect and enhance important shareholder rights.”\textsuperscript{13}

On other ESG matters, Glass Lewis also declared:

- It will “generally support shareholder proposals requesting that companies provide disclosure concerning the diversity of their workforce. . . .”\textsuperscript{14}
- “May consider recommending that shareholders vote against members of the board who are responsible for oversight of environmental and social risks.”\textsuperscript{15}

In November 2019, Institutional Shareholder Services (ISS) released its *Proxy Voting Guideline Updates for 2020*.\textsuperscript{16} The report highlighted three issues for US corporations:

- **Independent Board Chair – Shareholder Proposals**: ISS will generally recommend a vote in favor of shareholder proposals requiring chair persons to be independent directors.
- **Share Repurchase Program Proposals**: ISS will recommend a vote in favor of management proposals to institute open-market share repurchase plans permitting shareholders to participate on equal terms.
- **Problematic Governance Structures – Newly Public Companies**: ISS will recommend a vote against individual directors or the entire Board should ensure that their companies have identified the most relevant stakeholder groups and that they have a robust strategy to engage with them.


\textsuperscript{14} Ibid.

\textsuperscript{15} Ibid.

\textsuperscript{16} Institutional Shareholder Services, *ISS Americas: Proxy Voting Guidelines Updates for 2020*. 
Boards need to ensure that they have a good understanding of their shareholders and make sure that strategies are in place for engaging retail shareholders, especially if they’re expecting a close vote. The SEC has underscored the importance of more retail participation in proxy voting and wants retail investors to be more informed about proxy matters. Technology can reduce the effort required to vote, helping retail investors participate more easily.

A variety of technological solutions can be utilized for engaging retail shareholders. Examples include these solutions:

- **Push Notifications**: Push notifications via text messages can alert retail investors who often put proxy materials aside with the intention of returning to them later but then fail to do so before the deadline. Firms can also “push” proxy information via media releases into retail shareholders’ news feeds through a variety of digital news outlets.

- **Enhanced Emails**: Firms can make email communications more appealing by including visuals, branding, more prominent calls to action and voting features, short videos featuring the CEO and board members, and educational information for retail investors. Secure emails are being sent to investors to access voting sites without the need for pins or special “control numbers.”

- **Virtual Shareholder Meetings**: These make annual meetings more accessible to a greater number of shareholders, while eliminating the need for the board to travel to attend the meeting. Most companies permit all interested stakeholders to attend virtually, although many do not permit nonowners to ask questions. During the 2019 proxy season, the number of virtual shareholder meetings rose by 15 percent over the prior year, according to Broadridge Financial Solutions, the largest communications provider.

- **Interactive Proxy Microsites**: Proxy microsites can be transformative because they make proxy documents more consumable, summarizing the essence of proposals in plain language. AI-based systems can learn investor’s content preferences and highlight the information they most want to see.

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23. Main Street Investors Coalition, “Retail Investors Front and Center for SEC Chairman Clayton,” posted on mainstreetinvestors.org, October 16, 2018.

24. Based on Broadridge’s 2019 ProxyPulse™ data. It covers the results of 4,059 public company annual meetings held between January 1 and June 30, 2019. ProxyPulse data is based on Broadridge’s processing of shares held in street name. The five-year trend data covers the proxy season, which is when the majority of public company meetings occur.
Board members should ask themselves or manage these questions before proxy season:

- Do we understand our investor’s current and evolving governance priorities?
- Are we doing enough to refresh the board and to address institutional investors’ recommendations on board diversity and tenure?
- Do we have a strategy for engaging our retail shareholders?
- Do we have appropriate time on our agenda to discuss the ESG matters most relevant to us—along with our stakeholder’s views on these issues?
- Have we identified the most relevant stakeholders to engage?
- How does our ESG disclosure compare to that of our peer group? Should we disclose metrics that track progress?

board if boards (a) adopt bylaws or charters that are materially adverse to shareholder rights, or (b) implement multiclass capital structures having unequal voting rights without a sunset.

Board members also need to be aware of the Proxy Advisor Interpretation and Guidance issued by the US Securities and Exchange Commission (SEC) in August, 2019. The SEC now requires greater disclosure from proxy advisors on any potential conflicts of interest, as well as higher standards of accuracy around the recommendations they provide. Voting advice is considered a solicitation and as such there could be liability for materially false and misleading statements.17

ISS has sued the SEC over its new regulations.18 Some advocates fear that the outcome could have a significant impact on proxy advisory firms’ ability to do their job. “We believe that the Commission’s new Proxy Advisor Interpretation and Guidance is likely to create substantially increased costs and unnecessary burdens on the process by which proxy advisors render their advice,” Ken Bertsch, executive director at the Council of Institutional Investors (CII), wrote in a comment letter to the SEC in October. “Among others, these include increased litigation, staffing and insurance costs that are almost certainly going to be passed on to institutional investors and their underlying retail clients.”19

Boards will need to monitor these regulatory developments.

Institutional Investors Stay Focused on Board Diversity

Some leading institutional investors will publish their voting policies for the 2020 season in Q1. Board members need to fully understand how the governance priorities of their largest institutional shareholders are evolving.

State Street Global Advisors, for example, announced last spring that in 2020 it will start voting against all nominating and governance committee directors (not just the chair) at companies where they have concerns about gender diversity, and are unable to engage in “productive dialogue” with management.20

Since the introduction of State Street’s “Fearless Girl” initiative in 2017, the company says 423 firms added a female director, and 22 committed to doing so in the near term. “However, 57% of the companies that we identified have failed to take action.”21

BlackRock’s chair and CEO, Laurence Fink, has also made ESG a clear priority: “To prosper over time, every company must not only deliver financial performance, but also show how it makes a positive contribution to society.”22

Some directors and managers are looking to go beyond simple statements of purpose by disclosing the “progress metrics” they’re tracking.

In sum, shareholder engagement is the watchword for 2020, due to the nexus of constituents focused on environmental, social, and governance (ESG) issues. Interest in ESG is heating up among all stakeholders—particularly millennials, as well as major institutional investors and proxy advisers. Developing new and robust ways of engaging all stakeholders is key to addressing growing expectations for corporate societal impact. Boards that leverage technology to understand sentiment and improve communications will be better positioned to meet rising expectations.

21 Ibid.