NEUBERGER | BERMAN

NB Votes: The 2022 Proxy Season

In this challenging economic environment, we believe that quality corporate governance is crucial to creating shareholder value—and that active investment managers have a vital role to play on behalf of their clients.

As geopolitical turmoil, persistent inflation and rising interest rates roiled markets in 2022, our investment teams again made their voices heard with our NB Votes initiative. Now in its third year, NB Votes aims to share our opinions by pre-announcing our proxy-voting intentions on an array of voting topics that, we believe, have material economic consequences for our clients (see graphic on following page).

NB Votes has three main goals:

- Encourage companies in which we invest for our clients to improve their governance practices, thereby enhancing long-term value our clients
- Improve the transparency of our voting process
- Demonstrate how our long-term, active-management approach drives our voting decisions

Meeting those goals often means going against the grain: In 2022, we announced our voting intentions on 63 key votes and sided against management on 54% of them, compared with announcing 60 votes and pushing back on 52% in 2021.

In this latest proxy season, we focused on proposals addressing a host of issues—from board independence and ESG oversight, to incentive schemes and capital allocation—that we believe ultimately shape companies' long-term financial performance.

Governance and Engagement Principles

Strategy	Incentives	Board Independence
Transparency and Communications	Shareholder Representation	Capital Deployment
Risk Management	Environmental Issues	Social Issues

This paper offers a sampling of NB Votes across key themes from the 2022 proxy season. All our views are founded on the conviction that active engagement is essential to helping deliver long-term value for clients—and while we acknowledge that our votes may not trigger immediate policy shifts, we believe our practice of regularly pre-announcing our intentions promote better shareholder engagement and send a strong signal about the direction we'd like companies to take.

KEY THEMES FROM THE 2022 PROXY SEASON

- **Governance improvements.** Neuberger Berman believes sound governance structures and practices are foundational to creating value for shareholders while also protecting their interests. This year, we were pleased to see several companies in various sectors respond to investor demand for improved governance practices.
  - Netflix, Constellation Brands, Berkshire Hathaway, Tootsie Roll, Warby Parker
- **Evolving structure of executive compensation plans.** Two incentives-based trends caught our eye. First, more companies granted one-time awards to cope with macroeconomic uncertainty, competitive labor markets and ongoing impacts of the Covid-19 pandemic; in our view, one-time awards are a source of concern, particularly when they lack rigorous performance objectives and are outsized relative to peers. On a more encouraging note, we also noticed more companies explicitly synching compensation to long-term strategic objectives.
  - Las Vegas Sands, Evoqua Water Technologies Corp., General Motors Company
- **Board-backed climate-related shareholder proposals.** We've identified climate change as a systemic risk to companies across sectors and geographies. As a result, we believe that companies should consider the long-term climate impacts of their business models, and that all issuers should be able to identify key environmental risks to their business. A few U.S. company boards supported proposals to address climate risks—a rarity in the U.S.
  - Boeing Company, Caterpillar Inc.
- **Importance of board-level oversight of material ESG issues.** Neuberger Berman has a longstanding belief that material ESG factors are important drivers of long-term risk and return—which is why we encourage companies to effectively monitor and manage material ESG risks factors and provide transparency to shareholders on these efforts. Starting this year, we implemented a new voting guideline where we may hold the chair of the Nominating and Governance Committee accountable if a board fails to establish oversight of material ESG matters.
  - Costco Wholesale Corp., Bunzl PLC

- **Transparency and communications.** We believe good governance and clear disclosure must go hand-in-hand on everything from capital allocation to carbon emissions. At many companies, however, transparency remains a work in progress.

  – Amada Co., Monster Beverage Corp., Union Pacific

THE VOTES

Governance improvements

Netflix: Implementing majority-approved proposals

Over the past several years, we have signaled our concerns about the company's failure to implement majority-approved shareholder proposals by writing letters to the board and opposing the reelection of directors. Since 2020 we have also disclosed our concerns—along with our voting intentions—ahead of the company's annual meetings. At this year's meeting, and in response to shareholder feedback, Netflix proposed to:

- Amend its charter and bylaws to declassify the board, such that each director will stand for annual reelection rather than a three-year term
- Adopt simple-majority-vote requirements
- Allow shareholders to call special meetings at a threshold of 20% of outstanding shares (as opposed to not having that right at all)
- Adopt a majority-vote standard for director elections and a market-standard director-resignation policy (meaning that directors who receive less than 50% of the vote must submit their resignation, which the board can either accept or reject)

Constellation Brands: Adopting one-share, one-vote class structure

The company's controlling shareholder announced an offer to convert its Class B shares with super-voting rights to Class A common stock at a premium. We backed the proposal—because we believe a dual-class structure doesn't maximize shareholder representation—and engaged extensively with the independent special committee of the board charged with evaluating and negotiating the agreement. Our actions included a letter to the committee detailing our support for the reclassification, though we also expressed concerns with the high cash premium. In the end, the board decided to collapse its dual-class structure and make additional governance improvements—including anti-pledging policies, majority-voting in uncontested elections, and the memorialization of the board's intention to rotate the lead independent director during the next regular election cycle.

Berkshire Hathaway Inc.: Appointment of lead independent director

In 2021, we withheld support for the Governance, Compensation and Nominating Committee and sent a letter to the board explaining our concerns that the chair of the board was non-independent and that a lead independent director had not been appointed. That fall, the independent directors named Susan L. Decker as lead independent director. We acknowledged that meaningful improvement and commitment to addressing shareholder concerns by supporting Ms. Decker's reelection in 2022.

Tootsie Roll Industries, Inc.: Problematic corporate governance practices

Despite our engagement efforts, Tootsie Roll has maintained a litany of poor governance practices—including the combined role of CEO and chair, without a lead independent director; plurality voting for director elections; lack of a provision for shareholders to call special meetings or act by written consent; and dual-class voting structure. Additionally, the company has failed to appoint a financial expert to its audit committee for several years. To communicate our numerous concerns, we opposed the reelection of the entire board.

Warby Parker, Inc.: IPO governance concerns

It's not uncommon for newly public companies to have sub-optimal board structures; however, we expect companies to improve their governance practices over time. We opposed the reelection of several directors at Warby Parker, which went public in September 2021, due to the presence of several problematic governance practices and structures. In particular, we encouraged the company to adopt sunset provisions to phase out its staggered board and dual-class voting structure, as well as appoint an independent chair, or at least designate a lead independent director.

Evolving structure of executive compensation plans

Las Vegas Sands: One-time awards

We opposed the executive-compensation proposal due to concerns with the short performance-measurement periods included in the one-time awards granted to named executive officers. In our view, longer measurement periods are most appropriate and effective to incentivize longer-term performance.

Evoqua Water Technologies Corp.: One-time compensation awards

While we typically oppose one-time compensation awards, we made an exception after engaging with the independent chair of the board to understand the Board's rationale. In this case, two-thirds of the awards were based on performance and included appropriate safeguards, including rigorous goals and a multi-year vesting period. Importantly, the company made a clear commitment to eschew one-off awards in the future.

General Motors Company: Alignment of plans with long-term strategy

With electric vehicles now a cornerstone of GM's long-term strategy, we believed there was an opportunity to tie compensation more explicitly to the company's EV objectives. Multiple engagements included sending a letter to the board stressing the design and disclosure of executive compensation plans that more clearly reflect GM's decarbonization efforts and its actual annual performance. In 2022, the board announced various improvements to align compensation with GM's electric-vehicle-production efforts, including:

- Rewards for GM North America (GMNA) EV Volume, GMNA EV Launch Timing, and GMNA EV Launch Quality will be added to the 2022 long-term incentive plan (LTIP)
- New EV-related metrics comprising 15% of LTIP
- Enhanced disclosure of factors used to evaluate each executive, including those pertaining to ESG performance

Board-backed climate-related shareholder proposals

Boeing Company: Expanding governance of climate risk

As the aerospace industry faces challenges from evolving climate regulation, this major jetliner manufacturer will play an increasingly important role in meeting those challenges. After engaging for several years with Boeing's senior management, board of directors and sustainability team, last year we successfully encouraged the company to update and expand the Governance & Public Policy Committee's responsibilities to include formal oversight of environmental stewardship and climate change. Boeing also issued its inaugural comprehensive sustainability report, including disclosure of Scope 3 emissions from the use of sold products and alignment with the Task Force on Climate-related Financial Disclosure (TCFD) framework. We believe Boeing can further enhance its climate practices and disclosures pertaining to target setting, climate-aligned lobbying and alignment of capital-allocation decisions, and thereby supported a climate-risk-management proposal alongside the board's recommendation.

Caterpillar Inc: Improving climate reporting

As part of its long-term strategy, Caterpillar remains committed to achieving meaningful sustainability objectives by offering innovative products and services. In 2021 we supported a shareholder proposal to align the company's climate reporting with the TCFD; disclose Scope 3 emissions data; and set emissions-reduction targets verified by a third party. Since then, the company has responded by enhancing its sustainability efforts. These include:

- Committing to report in line with the TCFD framework
- Committing to disclose Scope 3 emissions data in 2023
- Incorporating an ESG performance metric in its 2022 incentive plan
- Creating the new role of Chief Sustainability and Strategy Officer
- Disclosing a new goal to reduce absolute Scope 1 and 2 greenhouse gas emissions (GHG) by 30% between 2018 and 2030.

While Caterpillar has disclosed that it has set science-based reduction targets for its own operations, we would still encourage it to have its targets verified by a third party. We are pleased that the company has committed to further enhance its reporting and, consistent with the board's recommendation, supported a new greenhouse-gas-related proposal.

Importance of board-level oversight of material ESG issues

Costco Wholesale Corp.: Formalizing board oversight on ESG

At Costco's 's January 2022 AGM, we opposed the reelection of the chair of the Nominating and Governance Committee due to the board's historical lack of formal oversight of material ESG issues. In June, we were pleased when the company updated its charter to give the committee oversight of important strategic decisions, including "environmental, diversity and sustainability policies and initiatives, including climate-related risks and opportunities."

Bunzl Plc: Independent oversight of ESG issues

Building sustainable supply chains and helping reduce its customers' carbon footprints are key strategic objectives at Bunzl, which makes products for a variety of industries, from grocery to healthcare. In reviewing the company's corporate governance documents, we noticed that no independent directors were charged with oversight of material ESG matters. After engaging with the company, Bunzl committed to address our concern at the next board meeting. Given this commitment, we chose to support the reelection of the board chair, and in subsequent months, the board formalized ESG oversight within a designated board-level committee.

Transparency and communications

Amada Co., Ltd.: Inefficient capital allocation

A significant surplus of cash, marketable securities, cross-shareholdings and land assets has weighed down the company's 5-year average return on equity to a lackluster 5.9%. After many years of stymied engagement, Amada decided—for the second time in two years—to postpone its mid-term allocation strategy, citing uncertainties in the global macroeconomic environment. We expressed our dissatisfaction by voting against the reelection of the President to the company's board.

Monster Beverage Corp.: Clearer ESG disclosure

We expect issuers to provide robust reporting on their management of financially material risks and opportunities, including relevant ESG matters. After assessing the company's ESG disclosures, we decided to support a shareholder proposal calling for clearer reporting on GHG emissions and reduction targets. We encouraged the company to provide disclosure on emissions data and establish reduction targets verified by a third party. We also believe the company should align its reporting with the recommendations of the TCFD.

Union Pacific: Disclosure of EEO-1 data

We believe successful human-capital management is critical to long-term financial performance, yet there is often limited and non-comparable disclosure across companies with regard to workforce composition and other crucial policies. That's why we encourage U.S. companies to disclose their EEO-1 reports as a starting point and provide supplemental information on their workforce-composition and human-capital-management practices. Last year we backed a shareholder proposal for the mandatory disclosure of U.S. Equal Opportunity Commission workforce data (commonly referred to as EEO-1 reporting, submitted to the EEOC by larger employers), which passed with 86% support. Union Pacific responded by including EEO-1 data, prompting our support for the reelection of Lead Independent Director and Chair of the Corporate Governance and Nominating Committee.

LOOKING AHEAD

At Neuberger Berman, we believe sound corporate governance policies and transparent reporting are essential for navigating the cross currents of this challenging economy. That's why we will continue to urge companies and their boards to embrace best practices through our NB Votes program, while also assessing our own ability to identify the most salient issues and use our voice effectively.

Pre-announcement of proxy voting intentions may still not be common practice. Yet as an active manager with voting responsibility on behalf of our clients that is spread throughout our investment teams, we believe we are well positioned to continue serving our clients by encouraging companies to raise their governance standards and enhance their financial performance.

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