"SAY ON CLIMATE" — KEY CONSIDERATIONS IN IMPLEMENTING SHAREHOLDER VOTES ON CLIMATE

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As the momentum of shareholder engagement on climate-related matters continues to grow across the globe, including in Canada, these issues remain a key focus area for public companies. One of the tools that has gained prominence is the so-called "Say on Climate" vote, where shareholders vote on their company's climate policies.

The initiative, launched by Christopher Hohn, a British fund manager, in conjunction with his investment firm The Children's Investment Fund Management ("**TCI**"), was first implemented by Aena, a Spanish airports group, in 2020. Since then, several other blue-chip firms like Unilever, Glencore, and CN have followed its lead.

While there are many positive aspects to Say-On-Climate, such as enhanced climate disclosure, they also raise a number of practical considerations for directors and executives that could affect corporate strategy.

The Concept

Say on Climate has three core components. First, companies must disclose their greenhouse gas ("**GHG**") emissions consistent with recommendations of the Task Force on Climate-related Financial Disclosures ("**TCFD**"), an international body established by G20 leaders to improve the efficiency of these disclosures. Second, they must disclose a plan to manage those emissions. Third, companies must provide shareholders with an advisory vote on the plan and performance relative to such plan at their annual general meetings ("**AGMs**").

Not surprisingly, there have been divergent reactions in how public companies have approached Say on Climate. These responses can be broadly divided into two categories — management resolutions and shareholder proposals.

- **Management Resolutions**. In some cases, such as at S&P Global, management teams have themselves implemented Say on Climate with the support of their board of directors. These resolutions establish a policy for mandatory disclosure of GHG emissions, their climate action plan, and an annual vote at future AGMs.

- **Shareholder Proposals**. In other cases, shareholders have brought their own proposals urging management to implement a Say on Climate. Similar in content to management-supported resolutions, such proposals call upon the company to provide disclosure of their GHG emissions and climate transition plans, and an annual vote on the progress. For instance, a shareholder proposal submitted by TCI at Canadian Pacific Railway's ("**CP**") recent AGM was approved by an 85% vote in favour of the proposal. In the lead up to the meeting, the CP board of directors had recommended that shareholders vote for the proposal. However, in the case of Charter Communications, a US telecoms group, shareholder attempts to introduce a Say on Climate failed after management recommended against voting for the proposal.

Key Considerations

For companies that wish to provide their shareholders with a Say on Climate, directors and management teams will need to consider a number issues, including directors' duties, stakeholder expectations, and impact on business plans:

- **Consequences**. Boards should consider how a Say on Climate may affect their decision-making flexibility and impose obligations with respect to climate-related matters. While advisory resolutions do not necessarily bind the company, the board may consider that shareholders have expressed a view on the company's climate action plan and how this view interplays with the directors' duties.
- **Director Duties**. Boards should consider whether putting forward an advisory resolution is in the best interests of the company. Further, the board needs to consider how to allocate the company's current and future resources between achieving business objectives, implementing its climate plan and balancing its obligations to, and the interests of, its various stakeholders.
- **Control**. A management Say on Climate approach bypasses the need for shareholders to put forward the resolution and instead requires the board to propose the resolution, thereby maintaining greater board-level control. Boards should also consider the optics of accepting a shareholder-led Say on Climate proposal, as it may be interpreted as a sign of the board's openness to advisory proposals generally.
- **Timing and Climate Disclosure**. Some issuers held their first Say on Climate during the 2021 proxy season, while a few other issuers are looking to implement the vote during the 2022 proxy season. To make this effort meaningful, companies will also need to make sure they build in adequate time to publish the relevant climate-related disclosures.
- **Frequency**. Boards and management teams will have to decide whether to implement a regular Say on Climate vote. Unilever, for instance, shared its climate transition action plan in Q1 2021, ahead of its AGM on May 5, 2021. The plan will be updated on a rolling basis and Unilever will seek an advisory vote every three years on any material changes made or proposed to the plan.

- **Threshold**. A Say on Climate resolution requires a simple majority (50% + 1) of the votes cast at a shareholders' meeting. Similar to advisory votes on executive compensation (Say-on-Pay), if a resolution is approved with a relatively low level of support, this may indicate that the climate plan requires change and may create an expectation that the board will adequately respond to shareholder concerns in the following year.

Proxy Advisors

Glass Lewis distinguishes between proposals that involve additional disclosure by companies, which it strongly supports, and those that offer a shareholder vote on a climate plan, where it expresses uncertainty. It says that in 2021 it will generally recommend against management and shareholder proposals requesting that companies adopt a policy that provides shareholders with an annual vote on a climate-related plan. On other proposals, Glass Lewis states that given their broad variety, and the lack of standardization on how shareholders should evaluate these resolutions before voting, it will review each resolution on a case-by-case basis. Glass Lewis intends to codify its approach in advance of the 2022 proxy season.

ISS has stated that it is developing its approach to Say on Climate and shareholder proposals. Generally speaking, ISS tends not to support "Paris Agreement" proposals that request asset divestitures, but supports requests for analysis and disclosure on whether a company's strategy is realistically aligned with Paris Agreement goals.

Shareholder Proposals in Canada

Shareholders of Canadian companies can use the shareholder proposal provisions under federal or provincial corporate statutes to raise climate-related issues. For example, under the *Canada Business Corporations Act*, in order to be eligible to submit a shareholder proposal, the shareholder must hold voting shares equal to at least 1% of the outstanding voting shares or with a fair market value of at least C$2,000. A company that receives an eligible proposal is required to include it in its management proxy circular for the shareholders' meeting. The company's board determines whether to accept the proposal; however, an aggrieved shareholder may seek recourse from the courts.

As noted, CP's AGM provides a recent example of a Canadian shareholder led proposal. Going forward, CP intends to have its shareholders vote, on an advisory basis, on a climate action plan disclosing the company's GHG emission levels in a manner consistent with TCFD recommendations. CP shareholders will also vote on climate-action strategy, including any progress made year over year.

Concerns Remain

Some are skeptical of the implications of allowing Say on Climate votes, while others are concerned more generally with shareholder proposals. BlackRock has expressed concern that Say on Climate could shift accountability from boards to shareholders. Although advisory votes are non-binding in nature, BlackRock argues that in instances where a proposal is rejected by shareholders, "this approach has the potential to weaken board accountability if used in isolation. BlackRock believes it is the board's responsibility to oversee all risks to the company, including climate, and ensure appropriate reporting to shareholders." Critics also argue that companies with strong environmental track records could suffer by having their climate strategies put to a vote by inexperienced retail investors.

All told, there is pressure on boards and management of public companies to establish a link between responsibility, accountability, and sustainability. Whether Say on Climate is that link will depend on each company's circumstances, including its policies, initiatives, disclosures, and engagement with investors and other key stakeholders.

Learn about new developments in sustainability and how McMillan LLP can help you reach your ESG goals here.

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A Cautionary Note

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