Vanguard Investment Stewardship

U.K. Regional Brief

This Regional Brief reports on the corporate governance topics and trends Vanguard's Investment Stewardship team observed across the United Kingdom during the 2023 proxy year; it includes data on the proxy votes cast by the Vanguard-advised funds during the period.[1] We provide this brief, and other publications and reports, to give Vanguard fund investors and other market participants an understanding of the engagement and proxy voting activities we conduct on behalf of the Vanguard-advised funds.

Vanguard's Investment Stewardship team conducts proxy voting and engagement on behalf of the Vanguard-advised funds. Our approach to evaluating portfolio companies' corporate governance practices is centered on four pillars of good corporate governance, which are used to organize this brief: board composition and effectiveness, oversight of strategy and risk, executive compensation/remuneration, and shareholder rights.

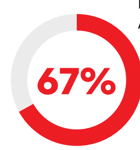
During the past proxy year (July 1, 2022, through June 30, 2023), the team conducted 152 engagements with 110 companies in the U.K., representing $80.8 billion in equity assets under management (AUM) engaged in the region. The funds voted on 11,105 proposals at 639 companies in the region.

At a glance

110 companies engaged	**152** total engagements	**639** companies where a proposal was voted on	**11,105** proposals voted on	**$80.8B** equity assets under management engaged

Regional AUM engaged

Percentage of regional AUM engaged



152 Total engagements in the region

$80.8B Total engaged equity AUM in the region

$119.9B Vanguard's total equity AUM in the region

1 Vanguard's Investment Stewardship program is responsible for proxy voting and engagement on behalf of the quantitative and index equity portfolios advised by Vanguard (together, "Vanguard-advised funds"). Vanguard's externally managed portfolios are managed by unaffiliated third-party investment advisors, and proxy voting and engagement for those portfolios are conducted by their respective advisors. As such, throughout this document, "we" and "the funds" are used to refer to Vanguard's Investment Stewardship program and Vanguard-advised funds, respectively.

Board composition and effectiveness

Our primary interest when evaluating a company's corporate governance profile is ensuring that the board of directors has the appropriate level of independence and mix of backgrounds, skills, experience, and diversity of personal characteristics to effectively provide independent oversight of management, company strategy, and material risks.

Director succession planning. We observed a renewed focus in the 2023 proxy year on board refreshment and succession planning among U.K. boards as they shifted away from a focus on near-term concerns related to the COVID-19 pandemic. In general, we observed that U.K. boards have high levels of board independence, with the only notable debate in this area centered on the tenure of board chairs. The U.K. Corporate Governance Code recommends that board chairs not remain in their posts beyond nine years from the date of their first appointment to the board. During the pandemic, several portfolio companies extended the board chair's term beyond nine years, but this year we saw boards working to clarify their recruitment and succession planning processes for the chair role and to assure shareholders that those processes were rigorous. In our engagements, some company leaders expressed the belief that certain shareholders would not support extending the chair's tenure much beyond nine years because of a strict interpretation of the U.K. Corporate Governance Code's recommendations. We continued to encourage boards to consider shareholders' long-term interests when contemplating board chair succession planning, ensuring that they have robust processes in place to find the right candidates and that they disclose progress in executing those processes.

Board diversity. During the 2023 proxy year, U.K. companies responded to nonbinding recommendations from the U.K. Listing Rules (released in April 2022) regarding gender and ethnic diversity on boards.[2] The "comply or explain" listing rules state that at least 40% of board members should be women, with at least one ethnically diverse director on the board. In addition, the rules state that at least one senior board position should be held by a woman. During the proxy year, we identified and engaged with companies that were not yet aligned with the U.K. Listing Rules' guidance to understand how their boards were accounting for those rules' requirements. In limited cases, the funds voted against Nomination Committee members where we assessed that the board had not taken appropriate steps and/or that disclosure was inadequate to address the U.K. Listing Rules' guidance. Overall, we observed that most boards appeared to be taking thoughtful approaches to updating their board recruitment processes to balance the requirements for diversity of personal characteristics with diversity of skills and experience.

Board effectiveness. We continued to see boards improving disclosure of board skills assessments, often in the form of a skills matrix, board evaluations, or both. During the 2023 proxy year, we frequently engaged with directors and company leaders on these topics to understand how boards were thinking holistically about improving their effectiveness to account for the recommendations of the U.K. Listing Rules as well as the growing need to oversee strategies and risks related to regulation, technology, and sustainability.

2 *FCA finalises proposals to boost disclosure of diversity on listed company boards and executive committees.* Financial Conduct Authority, April 20, 2022.

Notable votes from the 2023 proxy year include:

At **Dechra Pharmaceuticals**, a U.K.-based company that specializes in veterinary pharmaceuticals and related products, the Vanguard-advised funds supported the reelection of the chair despite noncompliance with ethnic diversity targets incorporated into the U.K. Listing Rules. Engagement with the board and company leaders allowed us to understand Dechra's public commitment to appointing a diverse director and the context around its approach to board refreshment plans. In January 2023, the board appointed a new diverse director as chair of the Remuneration Committee, thus aligning the board's composition with the U.K. Listing Rules' requirements.

Oversight of strategy and risk

On behalf of the funds, we evaluate board oversight and disclosure of material risks case by case, in accordance with each company's unique profile, taking into account the board's assessment of material risks and regional and sector-specific context.

During the 2023 proxy year, we continued to engage with U.K.-domiciled companies to understand their approach to emerging risks such as those associated with exposure to Russia and supply-chain interruptions resulting from the war in Ukraine, continued fallout from the COVID-19 pandemic, and human capital management practices heightened by the cost-of-living crisis and the increased competition for talent.

Sustainability-related risks. In 2023, for the first time, publicly listed U.K. companies were required to report in line with the Task Force on Climate-Related Financial Disclosures (TCFD). We observed companies across many industry sectors responding to evolving sustainability-related reporting requirements with a heightened focus on climate-related risks and disclosure. Climate-related risks and reporting remain a focus in our engagements with directors and company leaders in the U.K.

Say on Climate. The volume of advisory Say on Climate management proposals did not increase in the U.K. in 2023 from the 2022 proxy year. The Say on Climate management proposals that were put forward, though, garnered significant attention and some shareholder dissent. Although there is no established standard, regulation, or best practice to guide a company's approach to Say on Climate proposals, we interpret management proposals on this subject as a signal of shareholders' perspectives on the coherence and comprehensiveness of the reporting and disclosures a company provides to explain its climate plan. After analyzing each proposal and engaging with boards to understand their perspectives on emerging best practices on oversight and reporting of climate-related risks, the Vanguard-advised funds supported all management-proposed Say on Climate votes in the U.K. during the 2023 proxy year.

War in Ukraine. We continued seeking to understand boards' long-term approaches to identifying and overseeing key risks, including the ongoing response to the war in Ukraine and the resulting uncertainty in energy markets. We continued to encourage board oversight of long-term material financial risks and appropriate disclosure of those risks, in addition to the understandable attention being paid to current acute economic and political risks. Notably, energy market dynamics and supply-chain disruptions affected many companies across the U.K. We noted that at energy and utility firms, these evolving dynamics in some instances led companies to revise short-term emissions reductions targets. In those cases, we sought to understand how boards viewed those changes in the context of their long-term climate-related commitments and targets.

Notable votes from the 2023 proxy year include:

Shell plc and **BP plc**, both U.K.-based energy companies, received shareholder proposals requesting that each company align its 2030 Scope 3 greenhouse gas (GHG) emission reduction targets, specific to the use of energy products, with the goals of the Paris Agreement. Although we determined that the proposals addressed an area of material risk, following a case-by-case analysis of each proposal, we concluded that the actions requested in the proposals would require a change in company strategy. We believe that decisions about company business strategy and day-to-day operations are the responsibility of the company's board and management team. As a result, the funds did not support either proposal.

Executive remuneration

When reviewing executive remuneration, we assess how remuneration policies and practices are linked to long-term investment returns.

Quantum. We increasingly heard from directors of U.K.-listed global companies who struggled to attract and retain executive talent from the global marketplace, with a particular focus on competing with companies in the U.S., where quantum opportunity—the total magnitude of pay—is often much higher than in the U.K. We engaged with leaders of several companies to understand how their boards were approaching benchmarking exercises to triangulate executive pay figures in a complex global market, and how that approach aligned with their business operations and talent pool. Some directors and company leaders we engaged with expressed that they did not think some U.K. shareholders were receptive to higher pay amounts for global talent. We encouraged companies to prioritize long-term investment returns for shareholders in their decision-making processes and to provide reasonable disclosure of how they benchmark executive pay figures in the context of their operations and talent pools. We expect these conversations to continue at a number of U.K. companies given the increased public scrutiny of pay packages and regulatory changes aimed at encouraging more companies to list in the U.K.

ESG metrics. We observed a substantial increase in companies incorporating environmental, social, and governance (ESG) metrics into their executive incentive plans. Through our engagements, we learned that many companies felt they needed to incorporate such metrics based on guidance from a range of shareholders. We shared our perspective that we do not look for all companies to adopt ESG metrics, and that to the extent a company chooses to do so, the metrics should be rigorously designed, thoroughly disclosed, and tied to long-term performance goals related to strategic objectives or material risks. We found that companies were in various stages of defining measurable and material ESG metrics to incorporate into their remuneration plans. Although some metrics were relatively opaque and discretionary, or linked to nonmaterial issues, others thoughtfully reflected strategic priorities and investment returns.

Spotlight on health care

For most health care companies, material risks include product affordability and pricing, safety, ethical marketing, supply-chain management, and business ethics. Over the 2023 proxy year, we observed that many U.K. health care companies incorporated ESG metrics—with a focus on environmental issues—in remuneration plans. Several company leaders and directors shared that they were working toward including metrics that are material to the health care business, but they voiced challenges with measuring certain metrics.

Notable votes from the 2023 proxy year include:

At **Unilever plc**, a British fast-moving consumer goods business, the Vanguard-advised funds supported the remuneration report and policy put forward at the 2023 annual meeting. Unilever appointed a new CEO in 2023, giving him a significantly higher package than his predecessor. Some stakeholders expressed a preference for a phased increase in the new CEO's remuneration, given his profile before this role compared with his predecessor. The funds evaluate remuneration plan components, including quantum, case by case. This includes looking for salaries to be reasonably set—based on the role's scope, industry, and region—and benchmarked against an appropriate peer group. Our engagement with company leaders provided more context regarding the CEO's profile and the board's approach to setting his pay. Given that information, and a lack of historical concerns about pay-for-performance alignment at Unilever, the funds supported the remuneration report and policy.

The Vanguard-advised funds supported remuneration votes at the 2023 annual meetings of **Deliveroo plc** and **InterContinental Hotels Group plc**. Both companies proposed executive incentive packages that exceeded their U.K.-based peers in quantum. Both, though, provided strong and detailed rationales outlining their respective global talent pools and their approach to benchmarking. We engaged with leaders of both Deliveroo and InterContinental Hotel Groups ahead of their annual meetings to better understand how each company approached executive recruitment and succession planning in the context of global talent pools. We assessed that both companies positioned their quantum opportunities appropriately to deliver long-term investment returns while remaining cognizant of local market practice in the U.K. The funds supported the plans at both companies.

Shareholder rights

We assess structures that boards put in place to allow shareholders to effectively exercise their foundational rights.

Multiple share class structures. In late 2023, we engaged with industry associations and regulators to share our perspectives on proposed changes to the U.K. Listing Rules that would include making it easier for companies to list in the U.K. with multiple classes of stock with different voting rights. In a comment letter on a consultation for the proposed changes, we encouraged the U.K.'s Financial Conduct Authority to balance the desire to incentivize new listings and promote increased capital flows in the U.K. with the need to safeguard long-term shareholder interests. We will continue to engage with companies on the potential effects on shareholder rights resulting from the the U.K. Listing Rules changes, which are expected to be finalized at the end of 2023.

Proxy voting data

In aggregate, the Vanguard-advised funds supported a majority of management proposals in the U.K., driven, in part, by alignment between company disclosure and the U.K. Listing Rules, the U.K. Corporate Governance Code, and the Vanguard-advised funds' proxy voting policies. During the 2023 proxy year, we observed a rise in shareholder activism in the U.K., with a number of contested board elections and governance-related shareholder proposals. The funds supported several of these proposals following independent analysis of each one.

We also saw an increase in remuneration-related proposals, because of the three-year cycle for remuneration policy renewals. Compared with the prior year, in aggregate the funds supported more remuneration-related proposals in 2023 because of companies improving their disclosure and because we generally saw better alignment between pay and performance across portfolio companies. This had been an area of notable concern during the COVID-19 pandemic, when certain companies had negative financial results yet continued to pay out sizable incentives to executives, thereby weakening the link between pay and performance.

U.K.

		Management		Shareholder	
Alignment with our pillars	**Proposal type**	**Number of proposals**	**% for**	**Number of proposals**	**% for**
Board composition and effectiveness	Elect directors	4,492	98%	10	60%
	Other board-related	18	100%	8	88%
Oversight of strategy and risk	Approve auditors	1,201	100%	—	—
	Environmental and social	9	100%	3	0%
Executive remuneration	Management Say on Pay	866	97%	—	—
	Other remuneration-related	236	98%	2	0%
Shareholder rights	Governance-related	522	100%	—	—
Other proposals	Adjourn/other business	856	100%	—	—
	Capitalization	2,791	100%	—	—
	Mergers and acquisitions	89	99%	—	—
	Other	—	—	2	0%

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