Vanguard

Vanguard Investment Stewardship

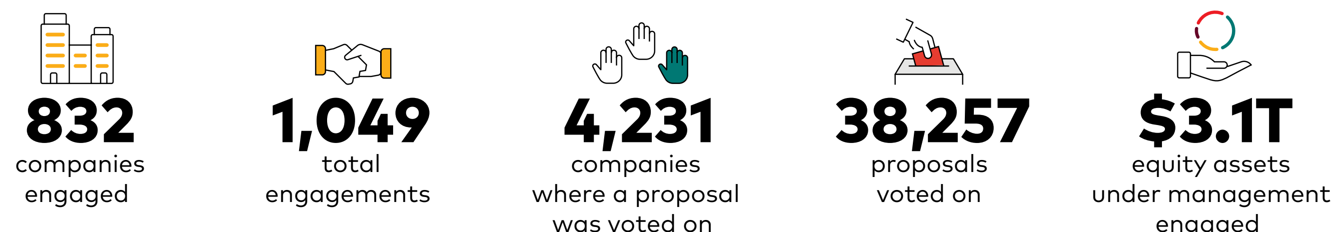
U.S. Regional Brief

This Regional Brief reports on the corporate governance topics and trends Vanguard's Investment Stewardship team observed across the United States 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 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 1,049 engagements with 832 companies in the United States, representing $3.1 trillion in equity assets under management in the region. The funds voted on 38,257 proposals across 4,231 companies in the region.

At a glance



Regional AUM engaged

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.

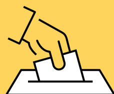
During the 2023 proxy year in the U.S., we engaged with portfolio company directors and executives on topics ranging from board and committee leadership refreshment to their onboarding processes for new directors. We saw many boards implement practices related to the universal proxy card (UPC) by increasing disclosure about their board skills matrices, director capacity and commitment policies, and board effectiveness assessments.

Universal proxy card and proxy contests. U.S. Securities and Exchange Commission (SEC) rules requiring the use of UPC in contested director elections took effect in September 2022, allowing shareholders to vote on the same ballot for a combination of directors proposed by either management or a dissident. As we shared in an **Insights piece** earlier this year, our approach to evaluating proxy contests remained the same with the implementation of UPC; we continue to focus on assessing the strategic case for change, the company's approach to governance, and the quality of director nominees.

Despite speculation across the market that UPC would lead to increased levels of activism, we observed that the volume of proxy contests in the 2023 U.S. proxy year remained relatively stable compared with the 2022 U.S. proxy year (25 contests in 2023, versus 23 in 2022). We did, however, hear anecdotally that a larger number of companies reached settlements to avert proxy contests. We will continue to monitor how UPC use in the U.S. market develops over time.

We heard from many company leaders that, in anticipation of the implementation of UPC, boards were working to improve disclosure of their board skills matrices. During our engagements, we encouraged company leaders to describe to investors how their boards' unique mix of skills and experience enabled each board to effectively oversee company strategy and material risks.

Director capacity and commitments. Across companies in the U.S., we continued to see boards self-governing their directors' capacity, with companies increasingly establishing director commitment policies and practices to ensure that directors can dedicate the requisite time and attention to each board on which they serve. On behalf of the funds, we assess director capacity and commitments case by case. Our process starts with looking to boards to disclose their director capacity policies, practices, and processes as an indicator of effective corporate governance. We continued to prioritize engagements with companies where we had open questions about director capacity. In discussions with directors and company leaders on this topic, and via company disclosures, companies were often able to explain factors that mitigated potential concerns regarding director capacity.



Notable votes from the 2023 proxy year include:

At the 2023 annual meeting of **CSX Corporation**, a transportation company, the Vanguard-advised funds supported the reelection of a director with significant board commitments. That director served as CEO and board chair of a publicly traded company and as a director on two additional public company boards (CSX and Ecolab). Under the funds' policy, a named executive officer (the CEO, for example) of a publicly traded company may be "overboarded"—meaning considered to have excessive board commitments—if they serve on three public company boards. The funds' support for reelection of the director in question was informed by our case-by-case analysis, incorporating the CSX board's disclosure of its formal and periodic board evaluation process, director commitment policy, and assessment of the director's performance.

On the other hand, at the 2023 annual meeting of **Ecolab Inc.,** a global provider of water, hygiene, and infection prevention services, the funds voted against the same director's reelection, as the company's disclosure and the associated engagement did not provide us with an understanding of the board's assessment of the director's performance nor its plans to monitor the director's capacity.

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 discussed with many company directors how boards undertake prioritization exercises to identify, define, and mitigate material risks to their companies, such as cybersecurity risks, operational risks, human capital risks, and postpandemic supply-chain risks. In addition, we engaged with U.S. company leaders on environmental and social risks where material to the company. Company leaders told us that shareholders continued to express interest in how boards are managing material environmental and/or social risks; we also saw that reflected in the range of shareholder proposals submitted on environmental and social topics.

Environmental and social shareholder proposals. During the 2023 proxy year, we saw a larger number of environmental and social shareholder proposals put forward for a vote at the funds' U.S. portfolio companies: 359, compared with 290 in the 2022 proxy year. The funds supported just 2% of such proposals in the 2023 proxy year (down from 12% in the 2022 proxy year). This decline is largely attributable to the volume

and nature of the shareholder proposals—driven, in part, by November 2021 changes to SEC guidance—and improvements in company disclosure.

The SEC has modified its interpretation of Rule 14a-8(i) under the Securities Exchange Act of 1934. For public companies that are subject to the federal proxy rules, this rule outlines exceptions to the inclusion of shareholder proposals in companies' proxy statements, subject to certain procedural and substantive requirements. The recent changes limited companies' ability to exclude proposals under the rule's "ordinary business" exception that relate to a significant social policy issue and also limited what may be considered "micromanagement" of a company under the exception, contributing to an increase in the number of proposals that may be immaterial at the company in question, direct company strategy or operations, do not provide sufficient discretion to company leadership to act on the proposal's request, or are otherwise overly prescriptive.[2]

We have also observed that, in recent years, many U.S. public companies increased their disclosure related to certain material risks, including material environmental and social risks, in response to shareholder interest. As a result, many shareholder proposals submitted during the 2023 proxy year went beyond requests for disclosure and instead sought specific actions from companies, including changes in company strategy or operations. In some cases, we identified that although a proposal raised a material risk at the company in question, the board had already demonstrated appropriate oversight of the risk and evidenced its oversight through robust disclosure or had practices in place that substantially fulfilled the proposal's request. In those cases, the funds did not support the proposals, because boards demonstrated that the risks were overseen and disclosed to the market. The funds also did not support proposals that went beyond disclosure and encroached upon company strategy and operations. We continue to believe that the strategies and tactics for maximizing a company's and its shareholders' long-term investment return should be decided by its board and management team.

During the 2023 proxy year, the number of shareholder proposals related to environmental matters rose 50% from the prior year (to 150 such proposals in the 2023 proxy year, up from 100 in the 2022 proxy year). Companies in the finance and energy sectors received the highest number of environmental proposals—33 and 24, respectively. The most common subject of those proposals was target-setting for greenhouse gas emissions. Other common proposal topics focused on climate lobbying and fossil fuel financing. On behalf of the funds, we evaluated the proposals case by case, assessing each on its merits and in the context of the facts and circumstances of the company in question.

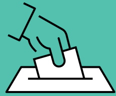
Across all sectors in the U.S., we saw companies receive shareholder proposals addressing social topics such as racial equity, reproductive rights, and pay gaps. The consumer sector drew the largest proportion of social proposals (it drew 99 of the 274 social proposals on which the funds voted), with several notable proposals in the sector concerning unionization and worker safety. We engaged with company leaders and directors to better understand how boards thought about these risks. For these proposals, too, we evaluated each one case by case on its merits and in the context of the specific company.

Despite changes in voting results, which are driven largely by the volume and substance of the proposals presented, our approach to evaluating shareholder proposals—including those on environmental and social matters—has been consistent over time. Our focus remains on identifying proposals that address financially material risks at a given company, supporting proposals that may fill gaps in the company's current practices (while not intruding on company strategy and operations) and providing sufficient latitude to the company on implementation.

Capitalization-related proposals. In the 2023 proxy year, the number of proposals the funds voted on related to company capitalization

2 See www.sec.gov/corpfin/staff-legal-bulletin-14l-shareholder-proposals.

rose significantly to 938, from 574 in 2022. This increase was driven, in part, by a rise in the number of reverse stock splits of companies seeking to avoid being delisted because of poor market performance. The health care sector—which significantly underperformed the broader market for most of 2022—accounted for much of this trend; of the 272 reverse stock splits in the 2023 proxy year, 58% involved health care firms. The biotech industry alone accounted for 30% of the reverse splits. The risks of being delisted are significant. The loss of access to public capital and decrease in liquidity can substantially affect a company's valuation. For these reasons, we believe it is important for companies to maintain compliance with exchange standards and preserve current investment returns.



Notable votes from the 2023 proxy year include:

As shared in an **Insights piece** in April, at the 2023 annual meeting of **Starbucks Corporation**, a multinational specialty coffee roaster, marketer, and retailer, the Vanguard-advised funds evaluated but did not support a shareholder proposal requesting a third-party assessment of the company's commitment to freedom of association and collective bargaining rights. Although we assess matters related to workers' rights as a material risk at Starbucks, the funds ultimately did not support the shareholder proposal because of the company's commitment to engage independent third parties to conduct a human rights impact assessment, inclusive of workers' rights. That fact, combined with our assessment that the board appeared to be taking appropriate steps to remediate and address the risks, gave us comfort that the board was appropriately acting upon the issues identified by the shareholder proposal.

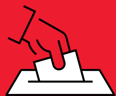
Executive compensation

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

In the 2023 proxy year, we prioritized engaging with companies where we had potential concerns about the linkage between the relative magnitude of executive pay and long-term shareholder returns. Beyond Say on Pay engagement-related activities, we observed an increased number of executive compensation-related proposals—from both management and shareholders. This increase was driven, in part, by the cyclical nature of "Say on Pay frequency" votes, requiring companies to seek shareholder input every six years on the frequency of the Say on Pay vote (annually, every other year, or every three years). As Say on Pay and the frequency vote were mandated by the SEC in 2011 for most companies, 2023 was the start of the third six-year cycle for many of them.

One-time awards. During the 2023 proxy year, we observed that companies continued to use one-time awards more frequently than they had before the COVID-19 pandemic. In many of our engagements, directors continued to cite retention concerns and recruitment challenges as the rationale for using one-time awards.

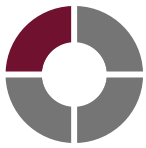
SEC Pay Versus Performance rule. In August 2022, the SEC adopted new rules requiring that companies disclose how executive compensation actually paid relates to the company's financial performance.[3] During engagements, company leaders and directors shared how they planned to modify their disclosures to improve the usefulness of their compensation-related disclosures to shareholders. On behalf of the Vanguard-advised funds, we support consistent, comparable disclosure.



Notable votes from the 2023 proxy year include:

At the 2023 annual meeting of **American International Group (AIG)**, the Vanguard-advised funds voted against Say on Pay because of concerns about the relative size of the pay program and the lack of performance conditions in a one-time equity grant. The CEO's five-year employment agreement provided for a $50 million special award of time-vesting restricted stock units. When evaluating these awards, we generally look for rigorous performance criteria as a requirement for vesting, as opposed to only the passage of time.

3 *SEC Adopts Pay Versus Performance Disclosure Rules*. U.S. Securities and Exchange Commission press release, August 25, 2022.



Shareholder rights

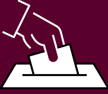
We assess structures that boards put in place to allow shareholders to effectively exercise their foundational rights.

Exculpation proposals. In August 2022, changes to state corporate law in Delaware—where the majority of U.S. companies are incorporated—enabled companies to include provisions in their corporate charters that limit company executives' liability. Such exculpation provisions were submitted for shareholder approval by over 250 companies, and the Vanguard-advised funds generally supported them after evaluating each case by case. We view the 2022 amendment regarding officer exculpation as a natural extension of the longstanding law allowing for the exculpation of company directors. Before the 2022 changes, shareholders often bore the cost of litigation, settlement, and increased insurance premiums associated with protecting company executives. The funds supported company charter changes when the proposals focused on exculpation and did not try to expand protections beyond the terms specified by law (for example, limiting liability for breach of loyalty, or for acts or omissions involving intentional misconduct or knowing violation of law).

Exclusive jurisdiction. A unilateral change to company bylaws that was particularly prevalent during the 2023 proxy year included an amendment to limit litigation activities to a specific legal jurisdiction. In engagements with numerous directors and executives, we heard the rationale that companies could limit legal expenses through the practice of focusing on one legal venue or a small subset of legal venues. Although such limitations could potentially impair shareholder rights, most of the proposed jurisdictions aligned to a company headquarters—a practice that we generally determined to be reasonable. Our initial assessment is that the benefit of efficiency that a company can gain from familiarity with a jurisdiction's local laws and practices outweighs the downside risk to a geographically dispersed shareholder base.

However, in cases where a company unilaterally adopts an exclusive jurisdiction provision in its bylaws, the Vanguard-advised funds would consider voting against members of the Governance Committee if the company's board is unable to explain a reasonable rationale for the change, and if we determine that the provisions intrude on shareholder rights.

Advance notice provisions. In part to defend against increased activism prompted by the universal proxy card—though such an increase, as noted earlier, has yet to materialize—many companies have changed their advance notice provisions. In our assessment, most of those changes have been reasonable from a shareholder rights perspective, with only a small subset appearing to be potentially onerous and intrusive on shareholder rights. Our perspective, on behalf of the Vanguard-advised funds, is that overly onerous advance notice provisions could infringe on shareholder rights and serve to entrench boards and company management in a manner that could present a risk to long-term investment returns. We look for boards to clearly articulate why they adopt certain restrictive provisions and why the benefits of the defensive posture may outweigh any resulting threats to shareholder rights. Examples of advance notice provisions that we view as potentially egregious include asking activist investors to disclose the names and holdings of their funds' limited partners (which are typically governed by partnership confidentiality provisions) and/or of their family members (beyond standard related-person definitions); any relevant special purpose investment vehicles; and the activist's prior and planned activities at other companies.



Notable votes from the 2023 proxy year include:

At the 2023 annual meeting of **ArcBest**, a logistics company, the Vanguard-advised funds voted against Nominating/Corporate Governance Committee members to express our concern about changes to the company's advance notice provisions. The bylaw changes required a nominating shareholder (and its affiliates) to provide details on any director nominee or shareholder proposals they have submitted to any company over the past five years, even if the proposal was withdrawn. In our assessment, the disclosure requirements were excessive and outside the bounds of market norms, and the unilateral action taken by ArcBest's board raised concerns regarding shareholder rights.

Proxy voting data

The volume of proposals voted on in the United States increased overall. We saw a larger number of management proposals (driven, in part, by Say on Pay frequency votes and officer exculpation proposals) and shareholder proposals (particularly environmental and social proposals). The funds' support for environmental and social shareholder proposals decreased from the prior year, primarily due to the changing nature of these proposals and the evolution of company disclosure.

U.S.

		Management		Shareholder	
Alignment with our pillars	**Proposal type**	**Number of proposals**	**% for**	**Number of proposals**	**% for**
Board composition and effectiveness	Elect directors	24,679	93%	44	18%
	Other board-related	360	96%	121	3%
Oversight of strategy and risk	Approve auditors	4,108	100%	—	—
	Environmental and social	—	—	359	2%
Executive compensation	Management Say on Pay	3,189	95%	—	
	Other compensation-related	3,145	84%	23	0%
Shareholder rights	Governance-related	463	90%	129	17%
Other proposals	Adjourn/other business	495	84%	—	—
	Capitalization	938	92%	—	—
	Mergers and acquisitions	195	98%	—	—
	Other	—	—	9	11%

Global

		Management		Shareholder	
Alignment with our pillars	**Proposal type**	**Number of proposals**	**% for**	**Number of proposals**	**% for**
Board composition and effectiveness	Elect directors	65,680	92%	3,684	91%
	Other board-related	14,124	83%	401	38%
Oversight of strategy and risk	Approve auditors	11,432	99%	—	—
	Environmental and social	34	94%	480	2%
Executive compensation	Management Say on Pay	7,129	88%	—	—
	Other compensation-related	13,561	87%	140	44%
Shareholder rights	Governance-related	11,545	76%	200	26%
Other proposals	Adjourn/other business	20,563	93%	—	—
	Capitalization	26,844	97%	—	—
	Mergers and acquisitions	7,203	97%	—	—
	Other	—	—	811	68%

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