

## Proxy Voting Report

Period: October 01, 2016 - December 31, 2016

Votes Cast	2056	Number of meetings	277
For	1827	With management	1820
Withhold	17	Against management	236
Abstain	3		
Against	207		
Other	2		
<b>Total</b>	<b>2056</b>	<b>Total</b>	<b>2056</b>

In 109 (39%) out of 277 meetings we have cast one or more votes against management recommendation.

# General Highlights

## **Special Issue - Board Composition**

Good corporate governance is essential to facilitating good corporate performance. It provides a framework for accountability between a company and its shareholders. Corporate boards are an important instrument in ensuring sound corporate governance. Failure at board level to sufficiently understand and mitigate risks was one contributing factor to the financial crisis of 2008, highlighting the strong materiality of poor corporate board oversight. The necessity of having the right skills in place at board level to compete becomes of even greater importance in light of the plethora of disruptive technologies, new business models, regulatory complexity and political uncertainty likely to be seen by companies in the coming years.

### *Taking a holistic approach*

With this in mind, as we approach the first half of 2017 when the vast majority of shareholder meetings take place, we highlight below the key points we assess when making our voting instructions for new and existing members of corporate boards. Robeco takes a holistic approach to assessing board composition, aiming to combine this with an understanding of the sector within which the company operates, local market corporate governance codes, examples of best practice and company history on issues of corporate governance. Therefore, whilst it is difficult to create a one size fits all best practice example of board composition, it is possible to outline some general points which we take into account when assessing board composition on a company basis.

### *Public disclosure: Making informed choices*

Maintaining a diverse balance of knowledge, experience, skills, age, background and gender, ensures that boards of directors reflect the reality of their operating environments and allow for proper strategic management of a business. However, transparency on this is the crucial starting point for testing board quality. In order to draw informed conclusions as to board quality, investors and other stakeholders must have access to accurate and complete information on the nominated candidates, the nomination process and the performance of the board.

Information on board members is not always readily available and much of what investors really want to know, for example how a board operates, takes place behind closed doors. Shareholders therefore have to rely on information provided by the company itself or, in some cases, on board self-assessments. Companies should therefore provide sufficient information for investors to understand the requirements in terms of skills and composition of a corporate board and the extent to which nominated board members meet these requirements. This allows investors to form informed opinions on board composition, resulting in better decisions when participating in shareholder meetings.

### *Board nominations: How deep is the bench?*

To achieve the right balance of tenures, experience, skills, expertise and other diversity criteria, it is important that the company has a strong and transparent nomination policy in place to guide the search for new board members. When a board proposes a new person to a board seat, it is crucial to understand the rationale behind the process that led up to the nomination being made, and what skills the board feels the new nominee will bring to the board. Robeco looks for nomination processes that address the following; 1) An independent nominating committee determines the required skills, attributes and board composition based on the business strategy.. 2) Based on these identified attributes and skills,

periodically a gap analysis should be performed. 3) Based on this gap analysis, a profile should be drafted for new board members. 4) When nominating new board members, it should be clear to shareholders what specific attributes a board member adds to the board. If the company does not disclose basic information on the nominees, we cannot vote in favor of nominees.

*Board independence: Maintaining effective oversight*

To achieve effective management supervision, it is imperative that the board can exercise independent judgment and is free of conflicts of interest. Corporate boards should be sufficiently independent to make sure that independent judgment has been applied in the boards' supervisory tasks and that they represent shareholder views. It is also important to strike a balance when considering independence. Indeed, there is a counterweight between having a board that is totally independent and having board members who understand the underlying operations of the business.

What is of overall importance is that the board is in a position to act as sparring partners for the management team, and that the CEO is accountable to a board composed of members who have sufficient understanding the business and the topics at hand, whilst possessing sufficient independence to oppose senior management when things go wrong. With this in mind, it is also essential that the board possess the tools to take action when things go wrong, including the power to terminate the CEO. This becomes problematic when the CEO of a company also chairs the board. Therefore it is Robeco policy to vote in favor of shareholder proposals that ask for separation of these roles.

In order to measure board independence it is also important for investors to understand the independence criteria which companies use when making new nominations to the board, as well as changing board composition in light of board tenures or related party transactions. Companies should therefore ensure they publish a robust policy on director independence with an extensive list of the factors they use to assess new and existing board members. On the whole, most companies disclose some sort of policy, but they vary considerably in their quality and extensiveness.

Robeco will therefore vote against nominated directors in such cases as when the nominated director is an insider or affiliate to the company, the board is not sufficiently independent according to local standards or when a more suitable director nominated by shareholders is available for election.

*Board diversity: Understanding the business*

When assessing board diversity prior to voting at the shareholder meeting of a company, we wish to see boards which are not only diverse across a range of metrics, but also reflect the diversity of the business, the challenges and the economic context within which it operates. These factors can differ per company, but it should be clear why the company focuses on selected factors. Nominations should be in line with the companies' diversity statement.

Robeco believes that a diverse workforce at all levels of the organization with equality of opportunity for all should support business performance, and therefore financial performance, over time. Concurrently, an ever greater number of companies are convinced that a well-diversified board adds value to the company. A common argument is that boards with people from different backgrounds are more

likely to approach issues from various perspectives, leading to more comprehensive decision-making and more effective supervision.

One such example of this is gender diversity. Recent studies by both Robeco and Morgan Stanley have connected gender diversity to financial performance. In fact, the former study found that that companies with a more diverse boards are indeed better positioned to outperform, whilst the latter found that the stocks of those American companies with the highest scores on diversity beat those scored the lowest by 2.3 percent on a monthly annualized basis over the last 5 years (2011-2016).

In addition, if the argument for increased diversity is that it adds value to the board, then boards must strive to also be diverse in the broadest sense, for example on nationality (to help in understanding the culture/geography of the organization), age and tenure (to balance new perspective vs understanding of business) and sector experience (to achieve a skill set which matches the underlying operations of the business). One such example comes from a 2012 study by the Association of Chartered Certified Accountants who found that, in analyzing board behavior, financial risk-taking was lower where board processes were characterized by a healthy degree of cognitive conflict, that is, differences of opinion over key company issues and board tasks. This is only possible where diversity of experience and opinion is present on the board. Over the course of the last year, Robeco has supported a several shareholder proposals asking companies to commit to greater levels of disclosure on diversity and pay equality.

#### *Self-assessment: Identifying necessary improvements*

In combination with a strong nomination policy to ensure that board members possess the right skills to perform their roles effectively, it is important the board regularly assesses their own functioning to ascertain where potential improvements can be made. Whilst shareholders are usually only given the chance to cast their votes on board composition at most once every year, it is important that they have an understanding of the how the board has functioned over the previous year.

This allows for a better assessment of new nominees, especially if skill or knowledge gaps have been identified over the year in review. We believe all boards should undertake regular self-assessments, and that these should be carried out on a yearly basis. An external party should be involved in the process of these assessments at least every three years to provide independent judgment. The results and follow up actions from these board assessments should be available to shareholders. Best practice in self-assessment can therefore be broken down into two steps: 1) performing an appropriate level of self-evaluation and 2) reporting to shareholders on these activities.

In this sense, regular monitoring and assessment is key in ensuring good corporate governance and effective risk management oversight. From a board perspective, this should entail regular assessments of the boards composition, organization, effective functioning and the identification of possible areas for improvement. Disclosing such information to shareholders allows for better informed proxy voting decision making. We therefore encourage all companies to disclose the results of their self-assessment process.

*Board composition: The role of investors*

The topics outlined above are just a few of the factors which result in our final voting instruction at a shareholder meeting. But a pertinent question to ask is what effect these votes have on the company in question. A recent (2016) study by PricewaterhouseCoopers highlighted the importance of investor engagement and proxy voting, and the subsequent impact which this has on board composition. As a result of investor engagement, 61% of surveyed directors say their board added a director with a specific skill set, 46% say they added a candidate who brought additional diversity of the board, and 24% say they added a younger board member.

The importance of informed proxy voting is therefore two-fold. Firstly, by exercising their shareholder rights, investors can help to ensure that the board in place post-shareholder meeting is the one that is best prepared and equipped to meet the challenges of the coming year. Secondly, by remaining open to engagement, investors can act as a sounding board for companies, sharing examples of best practice, in turn leading to increased shareholder value creation.

# Voting Highlights

## **Estee Lauder Cos., Inc. - 11/11/2016 - United States**

The Estee Lauder Companies Inc. manufactures and markets a wide range of skin care, makeup, fragrance, and hair care products. The Company's products are sold globally.

Robeco voted against the advisory vote on executive compensation at the 2016 annual general meeting of Estee Lauder, due to the significant one off awards with unchallenging performance conditions granted to the chief executive officer during the year. When voting on remuneration plans, Robeco pays close attention to their structure. It is essential that executives are being incentivized with the adequate award structures and metrics that are most appropriate for the company, based on their sector and strategy. However, when assessing the awards submitted for approval at the company's shareholder meeting, we see a number of significant issues, specifically around the granting of one off awards to the CEO.

Shareholders were asked to approve a payment of USD 30 million, in addition to the amount of USD 18 million due to the CEO under the agreed remuneration policy. In this case, we are extremely concerned that the USD 30 million award made to the CEO comes with extremely low performance conditions attached. Specifically, the awards vest based upon simple hurdles, with significant pay outs occurring simply for maintaining a positive net profit.

It is therefore possible that the majority of the one off award made to the CEO would continue to vest, even in light of significantly decreased company financial performance, so long as overall net profit stayed above zero. We therefore question whether such a sizeable award should be made without significantly more stringent performance conditions attached.

When considering the existing remuneration policy in place at the company, we also have some significant concerns. One such concern is the sole use of absolute metrics in the LTI plan which rather than rewarding executives for outperformance, can simply reflect economic factors or industry-wide trends beyond the control of executives, rather than the performance of management. In addition, the significant overlapping of performance conditions could lead to a high level of payout (or lack thereof) for performance against similar targets. We encourage the company to implement a compensation policy based upon a broader range of metrics, including some relative metrics, to more adequately align pay levels to company and individual performance. For these reasons, we voted against the advisory vote of compensation at the 2016 shareholder meeting.

At the shareholder meeting, the advisory vote on executive compensation received the approval of 92% of shareholder.

## **Oracle Corp. - 11/16/2016 - United States**

Oracle Corporation supplies software for enterprise information management. The Company offers databases and relational servers, application development and decision support tools, and enterprise business applications. Oracle's software runs on network computers, personal digital assistants, set-top devices, PCs, workstations, minicomputers, mainframes, and massively parallel computers.

At this year's annual general meeting, shareholders were asked to approve the advisory vote on executive compensation at the company. At the 2015 shareholder

meeting, the plan had received the support of approximately 48.1% of shareholders. As 27.21% of all shares are owned by co-founder and current Chief Technology Officer Larry Ellison, the investor support for this proposal is considerably low. This triggered the company to implement a number of changes surrounding executive compensation practices, including adding a new director to its compensation committee and changing the chair and vice chair of the committee, changing the principal partner at its compensation consultant, and performing an overall reevaluating compensation practices at the company. However, following an extensive review of this year's compensation practices, Robeco continues to oppose compensation practices at the company as we do not believe that the company's response to the sustained opposition of shareholders to its compensation practices has been extensive enough.

The company's lack of disclosure around the targets and maximum goals of the long term plan make it difficult for investors to sufficiently quantify whether the current levels of executive pay are appropriate when considering performance. When considering the overall amounts paid under the plan to senior executives, CEO compensation remains the highest in the sector, despite the company falling into the 65th percentile by market cap, and 37th percentile by revenue. We therefore question the ambitiousness of the targets set under the long term incentive plan. This is illustrated by the provision of the long term incentive plan that makes executives eligible to receive awards if Oracle underperforms the company's self-designed peer group. Almost half of the time vesting awards made under the long term incentive plan have also been granted in the form of stock options, which limit the downside for executives should performance suffer as the awards vest.

Robeco has consistently opposed compensation practices at the company, and we believe that the compensation committee have been deficient in their duty to shareholders in responding to the significant opposition by shareholders to compensation practices in recent years. For this reason, we also voted against the re-election three directors to the board, due to their stewardship of the compensation committee in the period concerned. In addition, we also voted against the re-election of two additional directors due to our concerns about the overall independence of the board. Both board members received significant compensation of the course of the year. Combined with their relatively long tenures on the board, we classify them as affiliated to the company, leading to an overall board independence level of 46%, below the majority requirement and significantly below established best practice. We also note the relatively long average tenure of board members at Oracle (14 years) as well as the relatively high average age (67 years) and will monitor these at the company going forward.

At the shareholder meeting, 49,23% of shareholders voted against the advisory vote on compensation. The nominees which we voted against were also all re-elected to board.

**Disclaimer**

Robeco Institutional Asset Management B.V. ('Robeco') distributes voting reports as a service to its clients and other interested parties. Robeco also uses these reports to demonstrate its compliance with the principles and best practices of the Tabaksblat Code which are relevant to Robeco. Although Robeco compiles these reports with utmost care on the basis of several internal and external sources which are deemed to be reliable, Robeco cannot guarantee the completeness, correctness or timeliness of this information. Nor can Robeco guarantee that the use of this information will lead to the right analyses, results and/or that this information is suitable for specific purposes. Robeco can therefore never be held responsible for issues such as, but not limited to, possible omissions, inaccuracies and/or changes made at a later stage. Without written prior consent from Robeco you are not allowed to use this report for any purpose other than the specific one for which it was compiled by Robeco.