Ethos proxy voting guidelines 2023: main changes

Ethos' proxy voting guidelines serve as a basis for Ethos' analysis of general meetings. The 2023 version has been validated by the Foundation Board in September 2022 and shall apply for all general meetings of covered companies (Swiss and non-Swiss listed companies) as of January 1, 2023.

Several amendments to the proxy voting guidelines are necessary due to legislative changes in Switzerland. A first part of the revision of the Corporate Law adopted by the Swiss Parliament in June 2020 came into force on January 1, 2021 and concerned only gender quotas in boards of directors and senior management, as well as transparency in commodity companies. On January 1, 2023, the remaining provisions of this revision will come into force. Companies will have two years to adapt their articles of association to this fundamental revision of the Swiss Code of Obligations (CO).

CHAPTER 1: DISCHARGE OF THE BOARD OF DIRECTORS

The rewording of point 1.2.b of the voting guidelines reflects a trend observed in recent years. In some countries, boards of directors have challenged and refused to place shareholder resolutions on general meeting agendas. For example, the supervisory board of Volkswagen refused to register a validly filed shareholder resolution asking the board of directors for greater transparency on lobbying activities. A similar case occurred at Total on a climate resolution. In such cases, Ethos considers that the refusal to re-elect the chairman of the board should be preferred. However, in some markets, the re-election of directors is not annual. It is therefore important to be able to sanction a board of directors that does not act in the interest of all shareholders.

CHAPTER 2: STRENGTHENING SUSTAINABILITY REQUIREMENTS

Ethos introduced a new point 2.1.e to strengthen the criteria for the approval of sustainability reports to properly reflect the actual performance of companies in meeting the targets set. Under point 2.3.g, a similar requirement is introduced for the approval of climate reports. Regarding climate strategy, Ethos strengthens its expectations by specifying that the company's 1.5°C target must be verified (e.g. by the SBTi) and that the company must explain in a transparent manner the measures to be taken and the contribution of each measure to the achievement of the target.

CHAPTER 3: BOARD OF DIRECTORS

Following various requests from members of the Ethos Foundation and to reflect best practices in corporate governance, as of 2023, the maximum accepted term of office for directors will be reduced from 20 to 16 years. This amendment reflects market practice and the need for regular board renewal, particularly to meet the requirements for independence and diversity (point 3.1.d). As it is the case today, potential exceptions are possible with clear explanations from companies such as the re-election of an important shareholder representative, founders or in case a transparent and public succession plan has been announced.

The new point 3.1.p will allow to refuse the re-election of the chairman of a key committee whose functioning is deemed unsatisfactory. This could be the case, for example, if the committee has not met or has met only once during the year.

As of 2023, Ethos will also closely monitor the key accounting assumptions and valuation of assets in the balance sheet based on climate risks. It is now widely accepted that climate change can have a major impact on the valuation of the company's assets. A critical review by the audit committee should therefore take place. For large greenhouse gases emitters, Ethos reserves the right to oppose the re-election of the chairman of the audit committee in case there is no evidence that such critical review has been conducted (point 3.1.k).

CHAPTER 4: AUDITING FIRM

A new point 4.1.k was added to allow Ethos to recommend refusing the re-election of the auditors if the audit report omits significant key audit matters. There is a growing consensus among investors that

ESG risks, such as climate risks, should be reflected in the financial statements, especially for large emitters of greenhouse gases. Thus, if the auditor does not mention climate change as a key audit matter when the company faces major risks, Ethos may, from now on, recommend to refuse the (re-)election of the audit firm.

CHAPTER 6: CAPITAL STRUCTURE

Under the new Corporate Law, the authorized capital will be abolished and replaced by the capital fluctuation margin. This new system allows the board of directors to ask shareholders for authorization to increase or reduce the share capital of the company within a certain limit during 5 years. The lower limit corresponds to 50% of the share capital entered in the commercial register, while the upper limit is set at 150%. The authorization in the articles of association may be granted for a shorter period of time and for different amounts. It is also possible to provide for an authorization only to increase or to reduce the share capital. The articles of association may always provide for a conditional increase of the share capital, which may not exceed half of the share capital. The conditional capital may be included within the limits provided for by the fluctuation margin or may exist in addition to the fluctuation margin.

The approach of the capital fluctuation margin tends to significantly reduce the control power of the shareholders by leaving more flexibility to the board of directors. At present, the authorized capital is only valid for two years and a capital reduction through the destruction of shares must be approved by the general meeting. With the fluctuation margin, the board of directors will be able to increase and reduce the share capital without consulting its shareholders, which raises concerns, especially in the case of a capital increase without pre-emptive rights or a capital reduction in companies where this could go against the interests of the stakeholders.

Ethos will therefore introduce a new point 6.2 in its voting guidelines to reflect the different requirements regarding the capital fluctuation margin. For the “increase” part of the capital margin, Ethos will set the upper limit at 20% of the issued capital, including a maximum of 10% without pre-emptive rights. For the "reduction" part of the capital margin, the lower limit will be set at 95% of the issued capital without adequate justification. An ordinary capital increase should be preferred in order to inform the shareholders about the purpose of the capital increase, in particular when pre-emptive rights are not granted. The same applies to a capital reduction through the cancellation of shares or through the reimbursement of part of the nominal value.

CHAPTER 8: AMENDMENT OF THE ARTICLES OF ASSOCIATION

The most important point concerns the possibility now offered by the Corporate Law to organize virtual general meetings. Ethos considers that the physical general meeting should be maintained and will therefore refuse the introduction in the articles of association of the possibility to hold online meeting only. Ethos considers that once the technology will be available, hybrid meeting should be organized.