Vanguard Investment Stewardship Insights

Voting insights: Climate-related proposals at Santos

Vanguard publishes Investment Stewardship Insights to promote good governance practices and to provide public companies with our perspectives on important governance topics and issues that come up for shareholder votes.

April 2021

Company: Santos Ltd.

Meeting date: 15 April 2021

Proposals: Item 6 (shareholder proposals) – Annual Vote on Adoption of Climate Report (Withdrawn Resolution); Capital Protection

Constructive engagement, votes cast/not cast

Before the annual meeting at Santos Ltd., one of Australia's largest oil and gas producers, we had a constructive engagement with company leaders about a "say on climate" proposal that would allow investors to cast an annual vote on a climate report. After listening to shareholder feedback, the board announced it would comply with the proposal's asks and the proponent withdrew the proposal. We viewed this as a positive outcome for long-term shareholders.

The Vanguard funds voted against a "capital protection" shareholder proposal that asked the company to disclose details of how it would wind down its oil and gas operations and assets in a timeframe consistent with the Paris Agreement goals.

Vanguard's principles and policies

Boards are responsible for overseeing a company's long-term strategy and any material risks. As part of our Investment Stewardship team's activities, we regularly assess how well a board of directors oversees the company's strategy and the board's own role in identifying, mitigating, and disclosing material risks that may affect long-term shareholder value. Climate change is just such a material risk to our investors' portfolios.

We look for companies to exhibit three key elements of sound climate change risk management:

- A climate-competent board that can foster healthy debate on climate topics, challenge management assumptions, and make thoughtful and informed decisions regarding these risks.
- Robust risk oversight and mitigation measures, including setting targets aligned with the Paris Agreement and integrating climate-risk considerations into strategic business planning and capital allocation decisions.
- Effective and comprehensive disclosures, both qualitative and quantitative, to show progress over time, preferably written in accordance with the Task Force on Climate-related Financial Disclosures (TCFD) frameworks.

Our previous Insights on this topic provides more details on our views for climate-competent boards, risk oversight and mitigation of climate issues, and key considerations for effective disclosure.

Engagement and voting history

Over the last several years, environmental activist groups in Australia have focused on getting the country's largest energy companies to develop and disclose plans on how they will decrease emissions. During that time, Santos and its peers have received similar climate-related shareholder proposals. Our previous engagements with the board have covered that topic, among other matters.

In 2020, the Vanguard funds voted against a proposal that asked the company to adopt targets to reduce its greenhouse gas emissions in line with Paris Agreement goals. At the time, we were encouraged by details that board members provided us on the progress the company had made on climate initiatives and its improving disclosures.

However, when speaking to the board members we shared our view that the proponent's requests were reasonable and we encouraged the company to make further progress.

Later that year, we were pleased to see the adoption of new, more ambitious targets, including a target of net zero emissions by 2040, and a target of 26%–30% emissions reduction by 2030 compared with 2019–20 for its own operational emissions.

Analysis and vote rationale

Before the 2021 annual meeting, we engaged with board members to discuss the capital protection and "say on climate" proposals.

"Say on climate" proposals are an emerging trend in various markets and sectors. We recognized the sensitivity of the topic and the potential material risk to the company's reputation among its investors, regulators, customers, and employees, and in the communities where it operates.

The company's initial view was that it did not consider an annual vote on its climate report to be necessary, given its existing targets, TCFD-aligned disclosures, shareholder engagement processes, annual votes on board directors, and a remuneration plan that includes emission-reduction targets.

Given Santos' strategic direction and the recurring activism from certain groups, we encouraged company leaders to view this vote as an annual accountability mechanism on this key material risk. We also suggested that the vote would be an additional tool for shareholders beyond engagement, thus increasing shareholders' rights and supporting alignment of interests.

After our engagement, the company announced it would adopt an advisory vote on its climate report at the 2022 meeting. We were pleased to see that the company was receptive to feedback from us and from other shareholders. Consequently, the proponent withdrew the resolution.

Our discussion also covered the capital protection proposal, which requested that the board develop a plan to phase out its oil and gas operations. We expect portfolio companies, especially those in the energy sector, to think through and develop responsible transition plans for certain assets. However, we believe boards and management are the leaders responsible for setting and deciding how to deliver that strategy, not shareholders. The Vanguard funds therefore voted against this proposal.

Finally, we also discussed the company's roadmap to net zero emissions by 2040, its reliance on carbon capture and storage to deliver on those targets, Scope 3 emissions, carbon pricing and scenario analysis, and how executive remuneration was evolving to reflect the new strategy.

We asked for more robust and detailed disclosure on how the company's capital expenditures were aligned with the goals of the Paris Agreement. We will monitor progress on all those fronts.

What Vanguard expects from companies on this matter

As mentioned above, we want boards to have appropriate competencies to oversee climate-related risks. We expect them to adopt robust risk management and mitigation practices, including emission-reduction targets. We also expect boards to push for the publication of comprehensive disclosures to the market on climate-related strategies.

INSANTOS_042021

Vanguard®