Vanguard Investment Stewardship Policy Insights

Vanguard's approach to board responsiveness

June 2023

The responsiveness of corporate boards to their shareholders—and other stakeholders—is a common topic of conversation in our discussions with portfolio company leaders and board members. This thematic Insight outlines how the Vanguard Investment Stewardship team, on behalf of Vanguard-advised funds,[1] thinks about the role a board plays in listening to and responding to shareholder perspectives.

What we look for on behalf of Vanguard-advised funds

Boards of directors are elected by shareholders, including Vanguard-advised funds, to serve in their collective best interests. As a result, we consider it to be a good governance practice for boards to provide channels through which their constituents can provide input and be responsive over time to feedback they receive. Shareholder perspectives and feedback can be shared with boards in different forms:

- Boards have always received shareholder input through votes cast on matters at their annual meetings. While the matters to be voted on cover a wide range of topics—and include proposals from both management and shareholders—the eventual votes are binary (for/against) and may lack the nuance or clarity of other channels.
- To supplement messaging through the proxy ballot, many companies also have a process for written communication to their board. For example, U.S. companies are required to disclose in their proxy statement whether, and if so how, communication with their board may be submitted.[2]
- More and more directors—often in conjunction with company leaders—are receiving input through engagement with shareholders. This may be, among other things, routine direct dialogue with a subset of stockholders, outreach either in preparation for or response to matters of concern, or engagement with proponents of a shareholder proposal.

Through each of these channels, we believe it is important for the full board to consider the messages received and evaluate them in the context of their fiduciary obligations to act in the best long-term interests of the company and its shareholders. We also believe it is good governance practice for boards to periodically disclose the aggregated perspectives they've received through various channels, how the board deliberated over and evaluated shareholders' feedback, what actions the board ultimately decided to take in response to shareholder feedback, and why the board believes such actions are in the best interests of all shareholders.

Responding to shareholder input

A company's shareholders may have unique values, preferences, priorities, and time horizons that result in divergent perspectives on the same underlying matter. As boards evaluate these potentially conflicting inputs, we believe their responses should remain anchored to their fiduciary obligations to

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.

2 https://www.sec.gov/rules/final/33-8340.html

serve as the stewards of the best interests of the company and its shareholders over the long term. Where advocates for a particular matter seek to advance an agenda other than the long-term value of a company, we encourage boards to hold fast to their obligations in the interests of all shareholders. While incorporating feedback from multiple vantage points may help to inform a board's decision-making process, we believe that boards of directors are generally best positioned to weigh the benefits, risks, costs, and tradeoffs associated with acting on individual pieces of shareholder feedback. The Vanguard-advised funds will generally defer to a board's judgement where matters are deemed immaterial to the long-term value of the company—even when they may be supported by a significant portion, but short of majority, of other shareholders.

The Vanguard-advised funds' policies

As noted above, we view appropriate responsiveness to shareholder perspectives as a fundamental part of directors' responsibilities. These perspectives may manifest themselves through votes in support of (or opposition to) the election of particular directors, an advisory vote on executive compensation, or a proposal submitted by company shareholders, among other matters. After developing an informed understanding of shareholders' views—often through outreach to and engagement with a critical mass of shareholders—we look for the board to take appropriate action, consistent with their roles as representatives of all the company's shareholders.

When a board fails to respond to a proposal supported by a majority of its voting shareholders and the Vanguard-advised funds supported the proposal, the funds will generally vote against relevant members of the board. For example, concerns with compensation matters would likely impact votes on members of the compensation committee, while governance concerns would generally impact votes on members of the nominating/governance committee. A pattern of unresponsiveness to shareholder feedback (e.g., a failure to act, or slow action, on shareholder votes) may be an indicator of poor governance practices and may result in increasing levels of opposition to board members' election.

We believe that all of this underscores the importance of ongoing communication between companies and their shareholders. Clear and comprehensive disclosure—of both corporate practices and shareholder perspectives—serves as the foundation of this dialogue. Ensuring that there are adequate channels through which shareholder perspectives can be gathered and then demonstrating responsiveness to those views aligned with the creation of long-term value for all shareholders is at the core of what we look for from the directors who serve on shareholders' behalf.

Vanguard publishes Investment Stewardship Policy and Voting Insights to promote good corporate governance practices and to provide public companies and investors with our perspectives on important governance topics and key votes. This is part of our growing effort to enhance disclosure of Vanguard's investment stewardship voting and engagement activities. We aim to provide additional clarity on Vanguard's stance on governance matters beyond what a policy document or a single vote can do. Insights should be viewed in conjunction with the most recent region- and country-specific voting policies.

The funds for which Vanguard acts as investment advisor (Vanguard-advised funds) retain the authority to vote proxies that the funds receive. To facilitate the funds' proxy voting, the boards of the Vanguard-advised funds have adopted Proxy Voting Procedures and Policies that reflect the fund boards' instructions governing proxy voting. The boards of the funds that are advised by managers not affiliated with Vanguard (external managers) have delegated the authority to vote proxies related to the funds' portfolio securities to their respective investment advisor(s). Each external manager votes such proxies in accordance with its own proxy voting policies and procedures, which are reviewed and approved by the fund board annually. The Vanguard Group, Inc., has not been delegated proxy voting authority on behalf of the Vanguard-advised funds.

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