SAGE ESG

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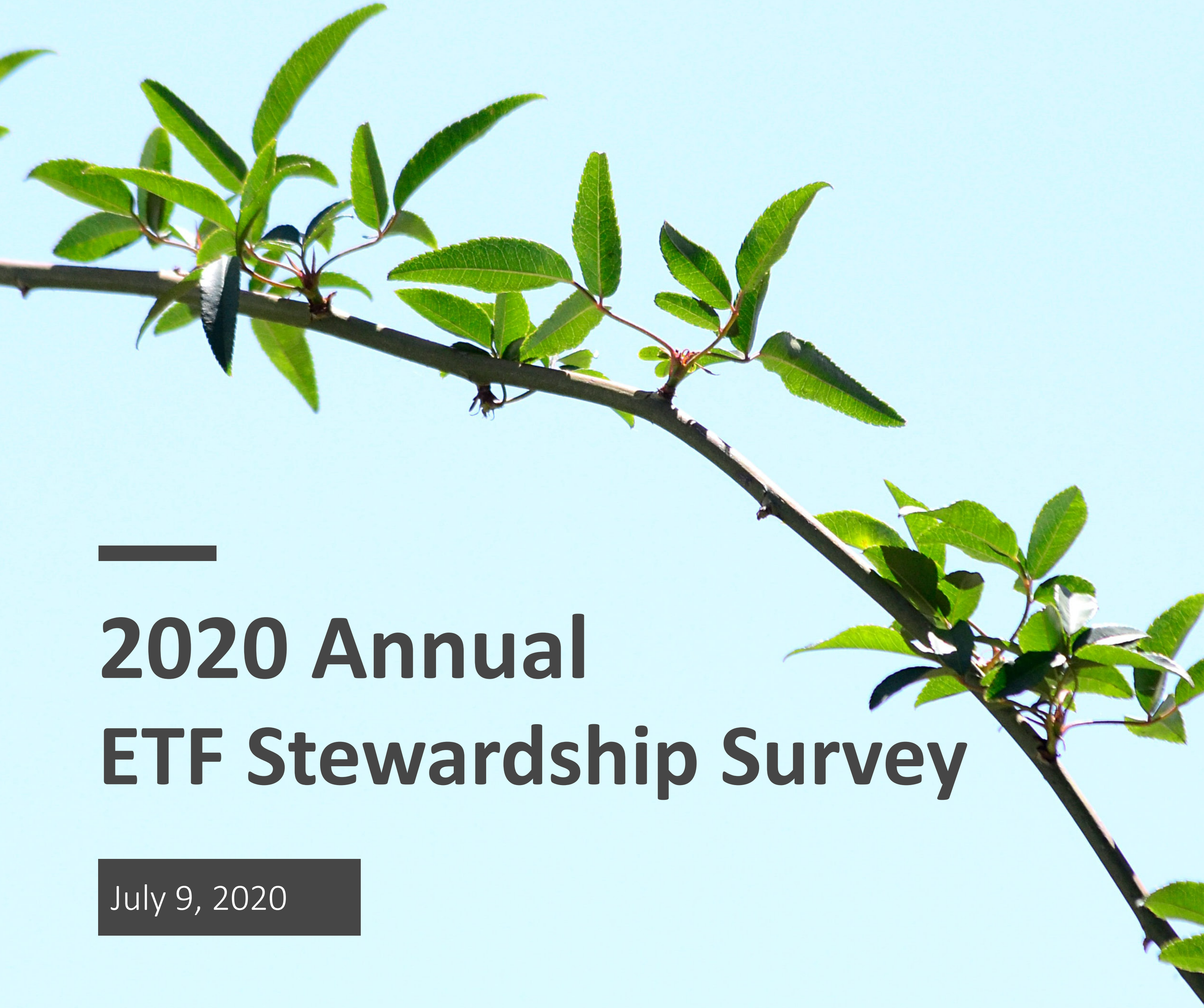

2020 Annual ETF Stewardship Survey

July 9, 2020

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by Robert Smith, Emma Harper & Sara Rodriguez

Sage conducts an annual stewardship survey to better understand how Sponsors of exchange traded funds (ETFs) are performing their duties as fiduciaries. The 2020 survey consisted of 28 questions designed to get at the very heart of not only policy, but also the existence of a verifiable and substantiated record of action. For each ETF Sponsor that was evaluated, we provided an overall letter grade based on their scores for each survey section, which included voting practices, engagement, disclosure, stewardship, and climate risk. With these grades in mind, we were able to create a preferred list of providers with which to invest.

What is Financial Stewardship?

In simple terms, a financial steward may be defined as an individual or organization who is of good character with the passion and discipline to protect the long-term interests of others. In this capacity they are committed to being a point of inspiration for moral, ethical, and prudent decision making. Competent financial stewards must be able to judge wisely and objectively based upon their seasoned knowledge and experience. Lastly, and perhaps most importantly, they must have a demonstrated ability to be independent leaders willing to correct unethical or illegal behavior for the benefit of all stakeholders. We believe that this notion of financial stewardship captures what most investors seek and expect from their investment managers.

In today's world, financial stewardship is being required and relied upon in ever greater quantities through a wide variety of investment modalities but none more important than the burgeoning market for ETFs.

It is our long-held view that investment management firms that provide ETFs to the investing public have enormous power and influence given to them by those who utilize their services. Indeed, by some estimates more than 80% of all assets that have flowed into investment funds in the past decade have gone to index funds.[1] This has meant that giant index fund ETF managers, such as Vanguard, BlackRock, and State Street Global Advisors, collectively own on average more than 20% of S&P 500 companies and control about 25% of the votes of the average S&P 500 company.[2]

Clearly, the level and quality of financial stewardship applied by these organizations should be of paramount importance because of the influence they may exert over the direction and development of corporate policies, industry trends, government regulation, societal behavior and, most importantly, the value of long-term investment outcomes. For all these reasons their financial stewardship truly matters.

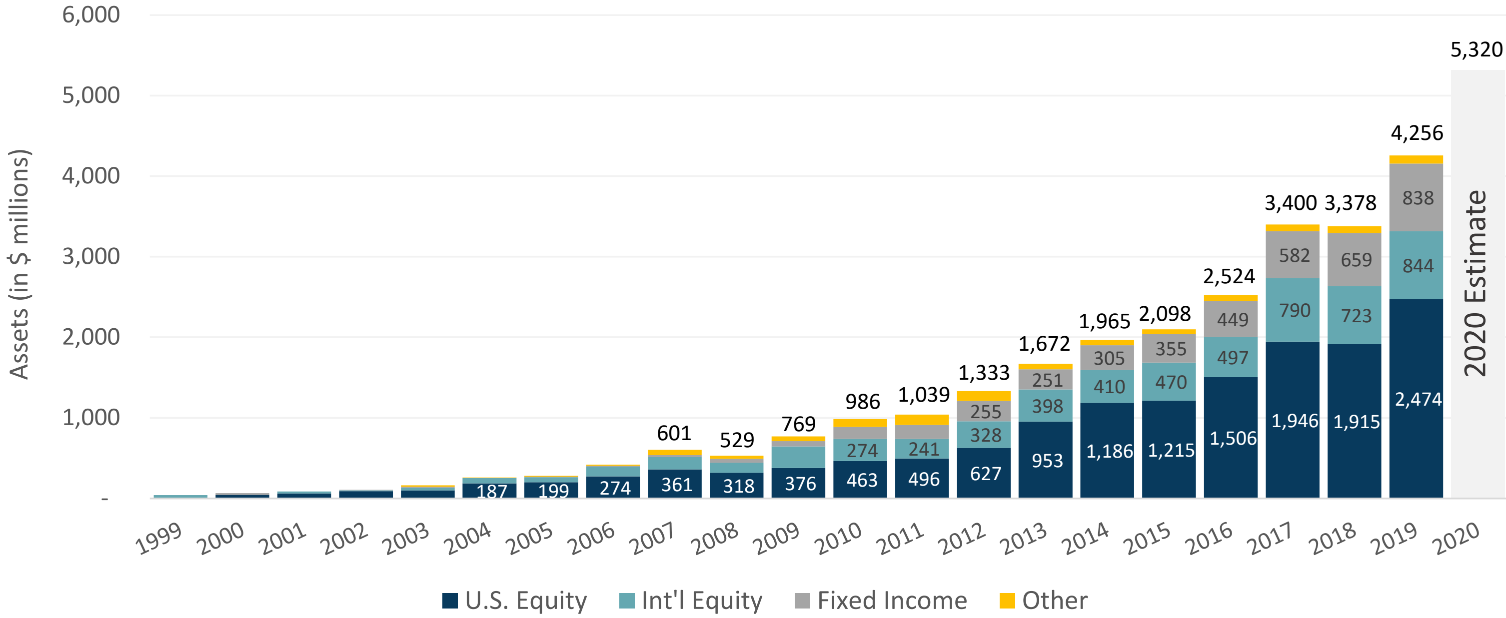
ETFs for All

U.S. ETF assets have been growing at roughly a 25% annual rate for the past 10 years. This market, which currently represent some 37% of the combined daily volume on all U.S. stock exchanges, is expected to reach $5.3 trillion in assets under management (AUM) by year-end, up from $770 billion in 2010, according Bank of America. Moreover, flows into U.S. ETFs are expected to grow tenfold by 2030, eventually reaching $50 trillion.[2]

These trends have largely been supported by the fact that ETFs have become a favorite mode of investing for most financial advisors and institutional investors. According to the Financial Planning Association's (FPA) 2019 Annual Survey, 88% of advisors and institutional investors use or recommend ETFs and, for the fifth year in a row, ETFs have been the most popular investment option among the 22 choices featured in the FPA's annual investment survey. Institutional investors have also participated in this growth with a fourfold increase in ETF investments over the last five years, bringing ownership to over 65% of the total ETF market at the end of 2019.[3]

While the investor rush to ETFs has been powerful, it has also been narrowing in many respects. According to a 2019 report from CNBC, the top 10 ETFs trading on U.S. exchanges accounted for 28% of total U.S. assets under management, with the top 20 U.S. ETFs

ETF Asset Growth



Source: Bank of America Global Research, December 11, 2019

accounting for nearly 40% of all assets in the space, up from 25% a decade ago.[4]

This means that passive investing has now taken over nearly half of the U.S. stock market as investors increasingly avoid actively managed funds in favor of passive index funds. It is also worth highlighting that a whopping 98% of all ETFs are passively managed and the top five ETF Sponsors (BlackRock, Vanguard, State Street, Charles Schwab, and First Trust) preside over 87% of the total assets in the ETF markets today.[4]

Survey Overview

Since 1998 Sage has been deeply involved with the ETF market as an institutional investor utilizing a variety of funds from a range of ETF providers. Through these activities, we have entrusted our client investment funds with a range of sponsors in varying degrees. Through our due diligence and assessment process, we have actively engaged and reviewed each of the leading ETF Sponsors on their investment process, security research efforts, and overall performance.

In recent years, with the rapid growth of the ETF market and the inherent expansion in voting power associated with these trends, we aggressively expanded our assessment efforts to fully explore a range of important financial stewardship and fiduciary issues with each ETF Sponsor. A few years ago, we formalized this process through our Stewardship Survey to gain a better understanding of how each ETF Sponsor developed and executed its core fiduciary policies and stewardship practices.

Participant Universe

We sent our 2020 Survey questionnaire to 14 ETF Sponsors and received a 100% response rate.

2020 Survey Respondents

- BlackRock
- DWS Group
- Clearbridge
- Northern Trust
- Goldman Sachs
- Invesco
- Janus Henderson
- Nuveen
- PIMCO
- J.P. Morgan
- Charles Schwab
- State Street
- VanEck
- Vanguard

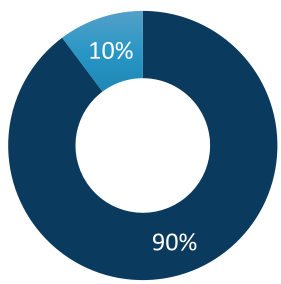
We wish to extend our appreciation and gratitude to our respondents. Without their support and information, this report would not have been possible.

Seventy-eight percent of the 2020 respondents participated in our 2019 survey and 22% had not previously participated. The combined $4.8 trillion in AUM of the surveyed respondents represented nearly 90% of the current U.S. ETF market.

U.S. Registered ETF AUM

■ Survey Respondents

■ U.S. AUM Not Covered by Survey

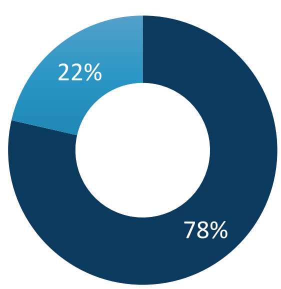


Almost 80% of our responses came from firms that would be considered "large," each with more than $950 billion in ETF assets under management. Additionally, 70% of the firms surveyed were publicly held companies with the balance being privately held entities.

Firm Size by AUM

■ Large firms (over $950 billion)

■ Small firms (under $950 billion)



At Sage, we strive to ensure that our clients are invested primarily with those ETF Sponsors that demonstrate service leadership, positive intentionality, adequate disclosure, and thoughtful policy execution. We believe these attributes are key to the quality and consistency of the proxy voting process.

2020 Survey Questions

Our survey examined five core areas of stewardship through the prism of 28 questions. This year, given the increased global attention on climate risk mitigation, we introduced a series of questions focused on this topic.

Survey Focus Areas (number of questions)

- Proxy voting policy, practices & record (9)
- Engagement policy, practices & activities (7)
- Climate policy adoption & execution (6)
- Stewardship resources & operating systems (4)
- Disclosure (2)

All responses were evaluated based upon the standards of practice Sage felt should be reflected on behalf of investors across the key focus areas. Most of the survey questions were designed to identify a simple "Yes" or "No" answer, and each ETF Sponsor was given the opportunity to provide additional information or details in support of the initial response provided.

Every question was assigned a one- or two-point maximum value, and poor responses received zero points. The level of importance for each focus area was identified by the number and depth of the questions posed in each section. Proxy voting was the most important consideration followed by engagement, climate risk policy, and lastly, stewardship resources. The maximum score value for responding to each of the survey questions was 46 points.

2020 ETF Stewardship Survey Questions

Voting Practices

1) Does (the Sponsor) have independent proxy voting policies?
2) Does (the Sponsor) have a proxy voting Advisor? If so, does (the Sponsor) follow the voting recommendation of the Advisor?
3) Are voting guidelines the same across all strategies, asset categories and geographic regions?
4) Does (the Sponsor) assess all non-routine voting activities?
5) How many of the ETF portfolio companies does (the Sponsor) exercise direct voting rights for? How is this decision made? Are there thresholds, i.e. minimum portfolio weight?
6) What is (the Sponsor's) percentage of votes in favor of versus against portfolio company management positions?
7) Does (the Sponsor) view a negative vote as a first or last resort to effect change in the portfolio company?
8) Do ESG related factors impact (the Sponsor's) voting behavior? If so, explain how.
9) Does (the Sponsor) engage in securities lending? If so, is there a threshold at which (the Sponsor) will not lend securities?

Engagement

1) How often does (the Sponsor) engage with ETF portfolio companies?
2) Does (the Sponsor) have a formal corporate engagement strategy?
3) What information does (the Sponsor) seek from engagement with portfolio companies? (Operating data? ESG Data? General information gathering? Policy voting intentions?)
4) What team at (the Sponsor) is responsible for corporate engagement activities?
5) Does (the Sponsor) join with other investors to share engagement information? If so, explain how.
6) Does (the Sponsor) participate in industry forums involved with Stewardship?
7) Post engagement, what is the time frame that (the Sponsor) will give the portfolio company to effect change? Are there metrics to determine the success of an engagement?

Climate Initiatives

1) Does (the Sponsor) monitor portfolio companies' oversight of climate related risks and or climate related opportunities?
2) Does (the Sponsor) review portfolio company overall governance practices? Does (the Sponsor) identify which directors or board level committees have been charged with oversight of climate-related issues?
3) What is (the Sponsor)'s voting record on climate related proposals? What is (the Sponsor)'s voting record on climate-related issues? Does (the Sponsor) follow third-party recommendations on climate-related voting?
4) Does (the Sponsor) generally vote for resolutions requesting portfolio companies to disclose information on the financial, physical, or regulatory risks they face related to climate change on its operations and investments or how the company identifies, measures, and manages risks?
5) Does (the Sponsor) vote for proposals requesting a report on GHG emissions, energy efficiency policies, and sustainability reporting?
6) Describe (the Sponsor)'s climate-related engagement strategies and scope.

Stewardship Professionals

1) Does (the Sponsor) have a dedicated Stewardship evaluation team? If so, how many professionals are on the team?
2) In the past 5 years, how many professionals have been added to the Stewardship team?
3) Does (the Sponsor) have a threshold for number of stewardship professionals in relation to number of holdings?
4) Are there any professionals with Stewardship certifications on the team?

Disclosure

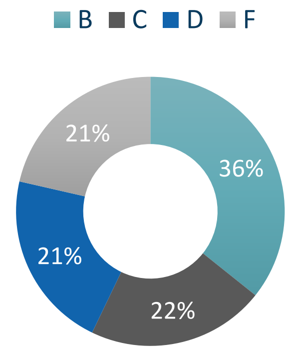
1) Does (the Sponsor) provide disclosures of voting records?
2) Does (the Sponsor) provide disclosure of engagements with individual ETF portfolio companies? If so, please provide examples of engagement with portfolio companies.

Survey Results

Upon completion of our response evaluations, we then determined a letter grade (A,B,C,D,F) for each respondent that reflected the relative strength of their respective answers within the peer group for the key focus areas. Each of the focus area grades were then combined to create the cumulative Sage Stewardship Grade for each respondent.

In general, we were pleased with the quality of the responses received from most providers, with 57% of them receiving an overall passing grade of C or higher; however, while several providers scored well in a few areas, we note that none of the respondents received an overall grade higher than B. The results illustrated in the following table suggest that most of the participants had room for some or significant improvement regarding their stewardship activities.

Overall Letter Grade



Company Grades

Grading Rubric	Public 1	Public 2	Public 3	Public 4	Public 5	Public 6	Public 7	Public 8	Public 9	Public 10	Private 1	Private 2	Private 3	Private 4
Overall Survey Grade	C	B	B	C	B	F	D	F	D	D	B	B	F	C
Voting Practices 16 Points	C	D	A	C	B	D	C	B	F	D	B	B	F	B
Engagement Section 11 Points	B	A	B	B	A	C	F	F	A	B	A	A	F	C
Stewardship Section 4 Points	A	A	F	C	F	C	C	F	C	C	F	C	F	C
Disclosure Section 3 Points	A	A	A	D	A	F	F	F	D	F	A	A	F	D
Climate Section 11 Points	F	A	A	B	A	F	F	F	F	F	A	A	F	C

Proxy Voting

According to SEC Chairman Jay Clayton, "Voting is a key component of shareholder engagement and investing more generally."[5] Since 2004, ETF Sponsors have been required to report their annual proxy voting records in SEC filings. By August of each year they are required to disclose how they voted over the previous year on both an individual ballot and fund basis. These records shine a light on how investment fiduciaries, managing trillions of dollars on behalf of fund investors, exercise stewardship.[6]

As more money has flowed into passive index funds and ETFs in recent years, it has put increasing downward pressure on investment manager fees. This has also led to an explosion in the number of proxies they need to process and vote in a relatively short time each year. April to June is a busy time for ETF Sponsors, with around 3,000 shareholder meetings taking place and tens of thousands of proxy votes needing to be cast. Consequently, nearly all institutional managers now must do more with less, which means fewer resources to dedicate to non-core functions like proxy votes.[7]

The last decade has also seen a marked increase in the number of shareholder proposals relating to environmental and social issues. Such resolutions have included proposals to increase climate risk reporting, limit political spending, report on gender pay disparities, and stop certain practices considered unethical to animals.[8]

These changing dynamics have made the use of proxy advisors an increasingly attractive option for institutional investors as a means of managing the proxy voting process.[8] In recognition of this growing trend, on August 21 ,2019 the SEC issued a Proxy Voting Guidance to provide affirmation and clarity to investment advisors about their proxy voting fiduciary responsibilities under Rule 206(4)-6 of the Advisers Act. This guidance also outlined the key considerations and corrective actions that investment advisors must enforce if they retain the services of a proxy advisory firm.

As the number of shareholder matters voted on has risen, so too has the proxy advisors' influence over voting outcomes. On this point, it is notable that ISS and Glass Lewis, two large proxy advisory firms, control about 97% of the market to provide proxy advisory services to institutional investors.[9] Given these circumstances, there is little doubt that these firms can and often do influence proxy vote outcomes as well as the overall corporate governance system.

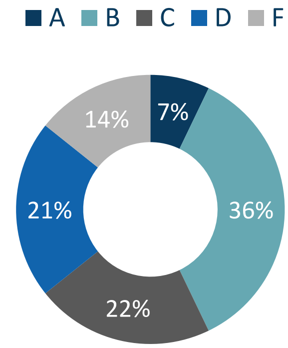
As a result of these trends, research suggests that institutional investors are bringing more shareholder proposals and voting with management less frequently today than in earlier periods.[10] Indeed, "For" votes on shareholder proposals relating to ESG issues are on the rise. In 2019, resolutions relating to disclosure on diversity received "For" votes 44% of the time, up from 13% in 2015; resolutions on human rights received "For" votes 30% of the time, up from 9% in 2015; and resolutions relating to gender pay equity disclosure received supporting votes 26% of the time, up from 7% in 2015.[11]

Following the record support for environmental and social issues in last year's proxy voting season, the 2020 season, with the backdrop of the coronavirus pandemic, has thus far seemingly created a stronger sense of commitment and urgency among investors for sustainable business practices. Indeed, this year there has been another record number of environmental and social shareholder resolutions that have passed with majority support.[12]

Voting Evaluation

The evaluation of voting policies and practices was guided by our consideration of the key tenets that promote and support optimal voting policies and investor/client outcomes. The survey questions on this subject were designed to provide the ETF Sponsor with an opportunity to identify the breadth and depth of their respective proxy voting policy features. The key focus issues that were reviewed and their relevance for investors are listed below.

Voting Grades



While each of the ETF Sponsors indicated that they had uniform firmwide independent voting policies in force, we noticed there were important differences in the methods each utilized to satisfy their voting responsibilities. Approximately 64% of the respondents received an overall passing grade for their proxy voting activities, a few did not, and several showed some signs of improvement from our last survey. The average grade received by this year's respondents was about a B.

Ideally, through our questions we were looking to gain a sense of the quality and consistency of each Sponsor's proxy voting process because that is what truly matters to ETF investors. We wanted each Sponsor to have established, well-described, independent proxy voting policies on all important corporate topics and issues that are uniformly applied across all funds. Generally, passive funds and ETF Sponsors maintain a more centralized system of proxy voting administration, leveraging the resources required for researching and executing votes across multiple funds.[13]

Focus Issues	Relevance
The existence of written proxy voting policies. Specific examples of proxy voting policies and practices that illustrate how decisions are made throughout the firm.	Written and clear proxy voting policies indicate a firmwide dedication to the protection of shareholder value and fiduciary responsibility to ETF investors.
Evidence of independent decision-making regarding voting decisions versus passively following recommendations of a third-party proxy voting advisor.	Independent decision-making when voting indicates the Sponsor has a voting policy and prioritizes voting on behalf of its ETF clients to help ensure optimal outcomes for the portfolio companies in which they are invested.
A Sponsor's exercise of direct voting rights for all portfolio companies or a demonstration of its strong intentions to do so.	The exercise of all direct voting rights demonstrates a Sponsor's commitment to a consistent application of policy preferences across all holdings within an ETF.
The Sponsor assesses and participates in all non-routine voting activities.	The assessment of all non-routine voting activities indicates the level and depth of a Sponsor's commitment to voting on all proxies on behalf of ETF clients.
Either written policies or specific evidence that illustrates that the Sponsor clearly integrates ESG factors within the voting process.	A Sponsor's acknowledgement of the importance of ESG issue integration within the voting decision process indicates an understanding of the material impact such issues may have on the financial outcome of the companies in which they invest.
Written and disclosed securities lending policies that identify the reasons and quantify the financial benefits for such activities.	Securities lending, while intended to be financially beneficial, can possibly add risk to an ETF portfolio and transfer investor voting rights away to the security lending counterparty. Sponsors that do not participate in securities lending do not have counterparty risk and retain all voting rights on behalf of their ETF clients. Some funds may use security lending to enhance fund returns but this marginal income comes at the expense of additional risk and a potential loss of voting rights on important investor issues.

For the most part, our respondents exhibited these practices, but our review of the published Proxy Voting Policy, Stewardship, or Corporate Responsibility Reports issued by a selection of the respondents indicated that they had in fact employed different proxy voting practices or teams for their active, passive, and ESG funds. Clearly, this is a concern since it brings into question whether or not all portfolio company votes are cast uniformly across all ETFs based upon a collectively conceived internal policy on important portfolio company business issues and ESG shareholder-sponsored ballot initiatives.

All our respondents indicated that they had independent voting policies and provided a general explanation of them. However, they also all indicated that they utilized external proxy advisors, with 80% indicating they had relied upon their advisors' recommendations within their voting process. Only 20% indicated that an advisor was used exclusively for proxy research services.

Half of the ETF Sponsors said it was their intention to vote every proxy, and 64% affirmed that they exercise their direct voting rights on all non-routine topics or issues. This was troubling because we believe ETF Sponsors should strive to independently review and vote all non-routine ballot proposals (such as mergers and acquisitions, the election of new directors, the issuance of common stock or related rights, and key executive compensation) for all company ballots currently held within their respective ETFs.

We were disappointed to learn that only 50% of the respondents voted in opposition to management ballot proposals more than 10% of the time. To some extent, this may be attributed to the exceedingly large volume of proxies that must be voted on by our respondents each year in a relatively short period of time. As a result of these pressures, ETF Sponsors are likely forced to focus their limited ballot research resources toward the largest and most widely held companies within their portfolios. This means that the investment managers must increasingly default to voting with management for the smaller and more thinly traded companies they may hold in their ETF portfolios. This poses a long-term concern for investors seeking investment managers that will strongly represent their stakeholder interests across all portfolio companies and demonstrate a willingness to take a more public stand through their respective votes on important corporate responsibility issues.

This year we asked the survey participants if ESG-related factors had any impact on their proxy voting behavior and if so, how? This was important because according to Morningstar research, over the last five years through 2019, there were 1,033 shareholder-initiated ESG resolutions that were voted on at U.S. company annual general meetings, an average of 207 per year. Furthermore, the research showed that five of the 10 largest fund families voted against more than 88% of ESG-related shareholder resolutions during this period.[14]

This suggests that ESG-sensitive investors should carefully evaluate the proxy voting records of the various ETF Sponsors because, as a group, the record suggests that the largest asset managers may be the least likely to support ESG shareholder-sponsored ballot initiatives. Given these research findings, we were a bit surprised to find that about 93% of our respondents indicated that ESG-related factors had a direct impact on their voting behavior, but only 64% offered any explanation of how and what ESG factors impacted their proxy decisions. It is our hope that the disappointing voting records cited by Morningstar and the positive ESG assertions identified in our survey responses will eventually be reconciled.

Lastly, as in the past, we examined each ETF Sponsor's policy on securities lending. This is an important issue because when a provider lends portfolio securities to other investors for a fee, they generally give up the voting rights for those shares for the period they are controlled by another party. In many cases investment managers can negotiate terms to retain the voting rights of those securities, but this is not commonly disclosed to investors. The income earned from securities lending, which most of the providers report, accrues to the ETF portfolio to augment investment returns. This year we found that roughly 64% of the respondents had active securities lending policies. This group was mostly comprised of the large ETF providers, and three of them indicated that their securities lending programs exceeded one-third of their existing ETF portfolio holdings. A couple of our respondents indicated that they did not participate in securities lending because they did not wish to deal with any possible counter-party risk or give up control of their proxy voting rights.

Engagement

Engagement is active ownership and an integral part of the financial stewardship process. In our view, it should not be treated as an appropriate substitute for proxy voting, but rather an important supplement to it. In this section of the survey, we wanted to gauge the frequency, depth, and methods of each Sponsor's corporate engagement activities. In our view, good stewardship comes from regular and sustained discourse with the management and related stakeholders of the companies that are held by an ETF. A strong engagement process demonstrates the Sponsor's efforts to uncover and mitigate emerging risks as well as seek long-term positive financial and ESG-related outcomes.

Our survey questions were focused on identifying and gauging each ETF Sponsor's:

- Formal engagement strategy
- Dedicated engagement team
- Time allocated to portfolio company engagement
- Examples of company engagement
- Disclosures of engagement findings
- Willingness to collaborate with other investors directly or through industry forums
- Metrics and time frames utilized to define engagement success

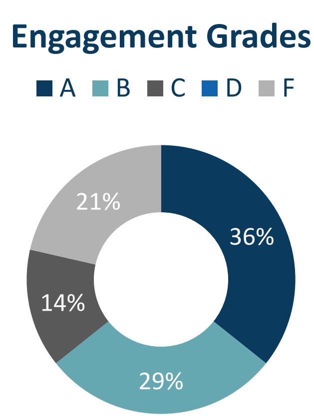
We want providers to engage with company management, have a formal corporate engagement strategy, disclose information discovered during engagements, and have concrete metrics to appropriately judge the successful outcome of engagements.

The responses received in this section varied greatly. While 78% of the respondents claimed they had a formal company engagement policy, most of them did not or could not provide an explanation of one. Surprisingly, roughly 20% to 25% of the respondents had neither a formal policy, an explanation of one, nor a formal schedule for such activities, and only half of the respondents offered any examples of their engagement activities.

We found this to be troubling because 78% of the Sponsors indicated that they had formed a dedicated company engagement team. The clear inconsistencies in these responses indicated that several of the providers were perhaps not as engaged with portfolio companies as they claimed. We also found that 57% of the Sponsors will indeed collaborate with other investors on their respective engagement efforts, and they all expressed a commitment to participate in relevant industry forums as a means of engagement.

We always look for ETF Sponsors to engage with their portfolio company managements and to have established, concrete metrics to appropriately judge the success of their respective processes. Over half of the respondents fell short of the mark with respect to identifying clear and discernible metrics for engagement success, and most failed to offer examples of their efforts or outcomes.

It is our belief that engagement should be part of the proxy voting puzzle rather than the entirety and these engagements should be, for the most part, open discussions. Unfortunately, many of our respondents opted to provide us with only a small amount of detail on their engagement examples with a limited percentage of portfolio companies. Some even cited that "private dialogue" was found to be the most effective driver of change in many situations. A few providers reinforced this notion by choosing to engage privately for a range of reasons. The need to keep confidential company information secure for competitive reasons was an excuse often cited for this practice.



Although 78% of respondents received a passing grade and 36% of respondents received an A, we believe there is significant room for improvement in the engagement policies and practices across all the respondents.

Unfortunately, ETF investors and other shareholders are often left in the dark on many conversations with portfolio company managements. This lack of full disclosure and communication with ETF investors may lead to frustration and distrust. We believe that, like proxy voting, transparency is the key to attaining investor trust and confidence, particularly when it comes to engagement with corporate managements on their behalf.

In this section we were looking to assess:

- The ETF Sponsor's internal guidance on climate-related voting and engagement
- Monitoring of portfolio company climate-related risks, disclosures, and reporting
- Systems in place to monitor corporate governance about climate-related issues
- Efforts to support or encourage board-level climate risk oversight committees
- Voting records on climate-related matters, particularly about shareholder ballots

Climate Risk

The beginning of 2020 marked the end of the world's hottest decade in recorded history.[15] Research suggests that capital market assets are losing in value, as markets continue to misprice climate-related risks that will manifest in a time period that is relevant to all investors.[16,17] Meanwhile, the 2020 Edelman Trust Barometer, the most comprehensive study of trust in the world, finds that almost three-quarters of 34,000 respondents in 28 markets want CEOs to speak out on climate issues and lead the way in delivering change rather than wait for governments to impose it.[18] The influence and power that investment managers hold through the investment capital they can provide to companies worldwide is pivotal to achieving meaningful climate change outcomes.

With these thoughts in mind, we added a new series of survey questions to evaluate each ETF Sponsor's approach to climate risk, their voting initiatives, and reporting requirements.

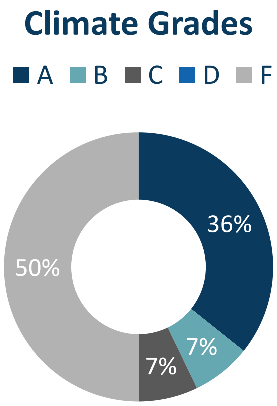
We found that 85% of the respondents were indeed monitoring portfolio company efforts to identify and manage climate-related risks within their respective businesses. Over half of the respondents (57%) also indicated they voted in favor of the maintenance or establishment of board-level climate risk assessment committees to help portfolio company risk mitigation efforts. However, only 50% of them voted in favor of further portfolio company disclosure on climate-related issues. This sentiment was further illustrated in the responses we received about greenhouse gas emission (GHG) and energy efficiency reporting initiatives, where only 36% of the ETF Sponsors voted in favor of such proposals.

Here again, several ETF Sponsors cited a preference for engagement and private dialogue to affect portfolio company climate risk mitigation. Unfortunately, too often we find that climate change engagement focuses on the disclosure of climate-related risks rather than strategic objectives and tangible outcomes. It is difficult for investors to know what in fact these activities achieve. For us, engagement lacks the force and conviction that voting requires.

The picture that emerges from our analysis is largely one of insufficient progress from the industry's most influential players. The focus of asset managers' engagement with companies remains firmly on the disclosure of climate-related data with fewer investors concentrating their stewardship efforts around corporate strategy alignment with the goals of the Paris Agreement and the setting of climate-related targets.[19]

Given the passive index orientation for most of the ETFs offered by our respondents, individual portfolio company divestment is not an option. They are therefore inherently long-term investors in their portfolio companies. As such, we were looking for formal climate-related policy commitments along with concrete measures to try and move toward greater portfolio decarbonization from our Sponsors.

Our grade distribution for this section shows that while many of the Sponsors demonstrated a rising awareness that climate change is a financial risk, many struggled with identifying their process to evaluate the risks that climate change poses to their ETF portfolios.



Stewardship Resources

With the sizable expansion of the ETF market over the last decade and the resulting growth in ETF Sponsors' fiduciary and proxy voting requirements, stewardship resources have become stretched. Managers have expanded their staffing resources dedicated to proxy voting and stewardship to help with the burden, but the numbers remain small as a percentage of assets under management or when expressed as a ratio of personnel time per portfolio company.[20]

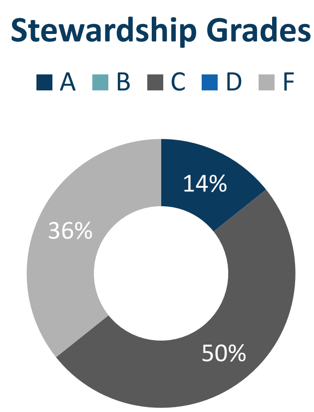
With these trends in mind we posed a series of questions in this section that were focused on determining the size, structure, and scope of the professional staff dedicated to fulfilling the Sponsor's important stewardship responsibilities.

As in our 2019 stewardship survey, nearly all the respondents had an established stewardship team tasked with the responsibility to shepherd the ETF Sponsor's proxy voting activities. They also affirmed that their teams had grown over the past five years. (We did not evaluate these staffing increases relative to each Sponsor's asset management growth to get a better understanding of their relative staffing adequacy, but this will be a feature of next year's survey.) Surprisingly, one Sponsor indicated that it did not have a designated stewardship team and did not provide any guidance on its stewardship staffing over the last five years.

The majority (64%) of the ETF Sponsors indicated that their teams featured investment professionals with special stewardship-related certifications. Some did not identify the exact number or what type of certifications they included but we gathered they were similar to last year's survey responses.

For those Sponsors that provided information about their teams, they indicated one or more of the following professional designations: CFAs, CFPs, EFFAs, FSAs, JDs, or CMAs. Additionally, some of the Sponsors had individuals that had received instruction or a certification from one or more of the following organizations:

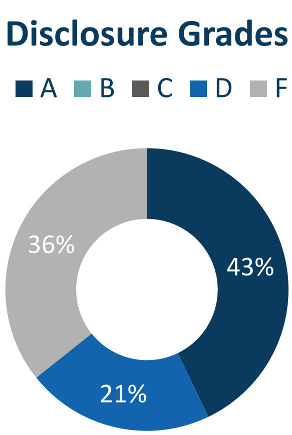
- Corporate Social Responsibility Reporting Certification UC Berkley
- The Forum for Sustainable and Responsible Investment (USSIF)
- Investor Responsibility Research Center Institute (IRRCi)
- The Sustainable Investments Institute (Si2)
- The Global Reporting Initiative (GRI)
- The Principles for Responsible Investing



Disclosure

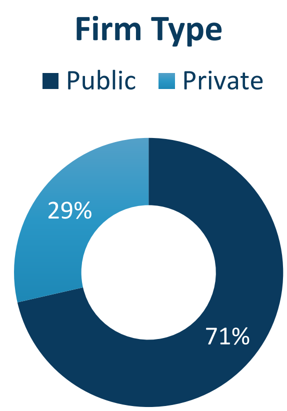
The last section of the survey focused on evaluating voting disclosure policies and dissemination of engagement reports. The full disclosure of an ETF Sponsor's voting and direct engagement records serves to protect the important fiduciary interests of ETF investors. Given the size and complexity of the average ETF portfolio there are a wide range of important corporate governance issues that investors must consider over time. Good disclosure also alerts investors to any potential misalignment of interests between themselves and the Sponsor on a variety of corporate management and ESG-related issues.

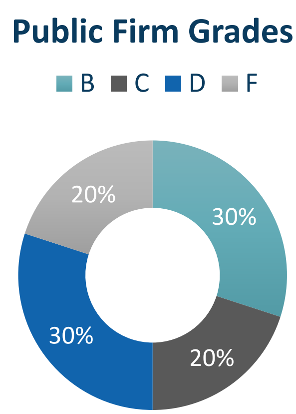
On the issue of public voting disclosures, we found that nearly all the respondents, with one exception, disclosed their proxy voting records. However, this was not uniformly so regarding the disclosure of company engagement activities. On this issue, 64% of the respondents disclosed such information, and of those, 35% gave hand-selected engagement examples and only 28% disclosed anonymous examples of corporate engagement reports. Given these results, we feel more needs to be done by ETF Sponsors to share information on their respective corporate engagement activities so ETF investors can develop a sense of commitment and direction on a variety of issues that may affect voting on current and prospective shareholder ballots in the future.

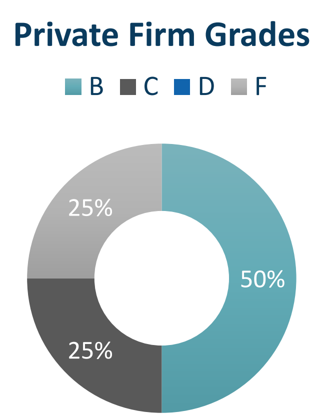


Public vs. Private Firms

This year's survey had 14 participants, 10 of the firms were publicly held and the remaining four were privately held organizations. Our Sponsor evaluations and grade distribution, which combined a firm's score for each of the five core areas, i.e. general governance, voting policies, engagement, professional support, and disclosure, revealed that 75% of the privately held firms achieved an overall passing grade, while only 50% of public firms managed to score as well. Although the private firms tended to have a less robust stewardship teams, several of the large public firms struggled with clearly identifying their voting policies and procedures as well as their climate risk-related policies or initiatives.

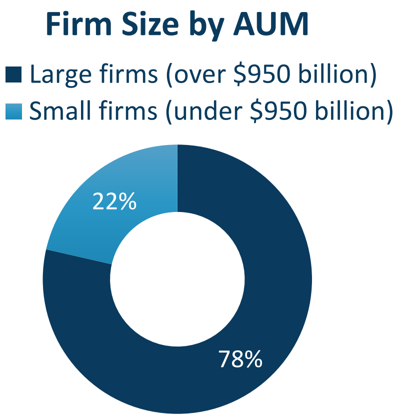


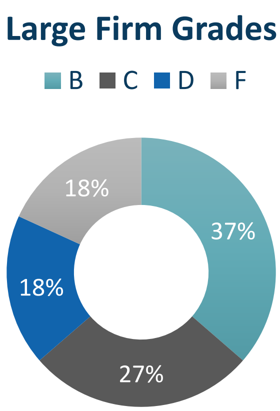




Small vs. Large Firms

The larger firms (>$950 billion in AUM) represented 78% of the survey respondents, and approximately two-thirds of this group achieved overall passing grades in our evaluation.

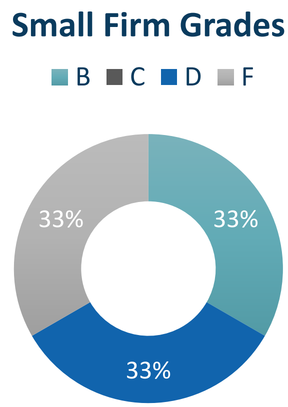




In most cases, we attributed these strengths to the size of the firm's human and financial capital resources devoted to proxy voting, issue research, and meaningful communication with their ETF portfolio companies. This seemed logical as they are often subjected to rigorous information and engagement requirements from investors, thus heightening their sensitivity for strong engagement practices.

Based on our findings, the engagement policies, practices, and corporate communication efforts of smaller, private ETF providers need to be intensified, more deliberate, and consistent to compete and deliver a more rewarding stewardship service to their ETF investors.

Finally, it should be noted that a small, publicly held ETF Sponsor achieved the best overall survey score. This illustrates that it is not just the amount of assets under management that determines the quality of the overall score, but rather the strong intentionality to emphasize stewardship throughout an organization. This was duly recognized in our assessment process because this firm demonstrated leadership, above-average standards of practice, and dedicated engagement capabilities.



2020 vs. 2019 Survey Results

Each focus area showed improvements for some respondents and deterioration for others. For most respondents, voting was the hardest section, with 60% of repeat respondents scoring lower than last year. Only 20% had an improved voting score, and 20% received the same scores as the previous survey.

There were various reasons for the drop in scores for many, including a predilection for voting with management on most issues, not exercising direct voting rights or not having the intentionality to exercise direct voting rights for all portfolio companies, using third-party advisors for more than research, and not assessing all non-routine voting.

The engagement section had a better outcome for most, with 60% of ETF providers receiving the same scores as last year and 10% improving; however, 30% saw their scores worsen, mostly surrounding their lack of transparency in the process.

The stewardship team focus area provided more mixed results, with 40% scoring the same as last year, 20% improving, and 40% worsening. The most common reasons for the lower scores this year were lack of metrics or explanation as to how the decision to add human capital to the team is made.

Lastly, the broad disclosure section had better results, with 70% of respondents scoring the same or better and only 30% worsening, with some lost points due to the lack of disclosure of engagements and lack of ease in locating voting records.

Footnotes

(1) Yi, Lun, "ETF assets to surge tenfold in 10 years to $50 trillion, Bank of America predicts" CNBC (12/12/19)

(2) Michael T. Cappucci, "The Proxy War Against Proxy Advisors" Harvard Management Co. (11/27/2019); Lucian A. Bebchuk and Scott Hirst, "The Specter of the Three", Boston University Law Review, Vol. 99,2019 pp.721-741

(3) Gurdus, Lizzy, "ETF assets rise to record $4 trillion and top industry expert says it's still 'early days'" CNBC (11/29/19)

(4) Tuckwell, David, "How institutional investors are using ETFs" ETF Stream (5/14/19)

(5) SEC Clarifies Investment Adviser's Proxy Voting Responsibilities and Application of Proxy Rules to Voting Advise, SEC Open Meeting Fact Sheet (August 21,2019)

(6) Cox, Jeff, "Passive investing automatically tracking indexes now controls nearly half the US stock market" CNBC (3/19/19)

(7) Cappucci, supra note 2 page 7

(8) Jon Hale, "Proxy Season Shows ESG Concerns on Shareholders' Minds" Morningstar (August 2019),

(9) Timothy M. Doyle, American Council for Capital Formation (ACCF), "The Realities of Robo-Voting" pub. On Harvard Law School Forum on Corporate Governance (November 29, 2017)

(10) Cappucci, supra note 2 page 38

(11) Hale supra note 8

(12) Jackie Cook and Jon Hale, "2019 ESG Proxy Voting Trends by 50 U.S. Fund Families", Morningstar, Inc., pub. On Harvard Law Forum on Corporate Governance (March 23, 2020)

(13) Cook and Hale supra note 12

(14) Cook and Hale supra note 12

(15) Dennis B. Freedman, A. Muyskens, J. "2019 Capped World's Hottest Decade in Recorded History", Washington Post (January 5, 2020)

(16) G. Steele, Confronting the Climate Lehman Moment: The Case for Macroprudential Climate Regulation, Cornell Journal of law and Public Policy. (2020)

(17) F. Reynolds, "Financial markets are mispricing climate risk" PRI (2019)

(18) Edelman, 2020 Edelman Trust Barometer

(19) Krystyna Springer, "Point of No Returns Part III-Climate Change" Share Action-Asset Owners Action Project (June 2020)

(20) Cappucci supra note 2

Sage Advisory Services

5900 Southwest Parkway
Building One
Austin, Texas 78735
United States

T +1 (512) 327-5530
esg@sageadvisory.com

Sage Advisory Services ESG Team

Emma Harper
Research Analyst

Andrew Poreda
Research Analyst

Sara Rodriguez
Research Analyst

Doug Benning
Data Analyst

Nick Erickson
Portfolio Manager

Komson Silapachai
Portfolio Manager

Bob Smith
Chief Investment Officer

Jessica McHugh
Director, Marketing Comms