SAGE ESG

Sage Advisory Asset Management

# 2022 Annual ETF Stewardship Report

## Every Vote Matters

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## Every Vote Matters

by Emma L. Harper

Passive investment vehicles such as exchange traded funds (ETFs) continue to dominate the investing landscape, with positive inflows of $406 billion in the first half of 2022.[1] The growth of the ETF market is largely due to the benefits these funds provide investors: diversification, access to the market, and liquidity. In fact, the average S&P 500 company has over 20% of its stock in passive vehicles.[2] What ETFs do not provide to investors, however, are ownerships rights, such as the ability to vote on company board oversight and engage with company management. Those rights belong to the fund managers, the largest of which hold a significant amount of market equity and the investing public's assets. For these reasons, it is imperative that investors understand how ETF providers are exercising ownership rights on their behalf.

As an asset manager, Sage has been using a variety of ETFs from a range of providers since 1998. This is our fourth year conducting our pivotal ETF Stewardship Survey. We designed this annual survey to gain a better understanding of how each ETF Sponsor has developed and executed its core fiduciary policies and stewardship practices. The largest ETF providers surveyed represent 7 of the 10 largest ETF providers in the US by AUM, and collectively our participants manage approximately $37 trillion in total assets and represent approximately 80% of global ETF AUM.[3]

Our survey, in addition to our due diligence work, contributes to positive changes in industry practices. Each year when the survey results are published, we share the results with the participants and offer to discuss their individual practices in relation to the broader peer group. We have been pleased by the positive response of participants and their willingness to engage and openly discuss best practice findings and possible improvements to their own processes. We seek to help providers and encourage them to continue progressing toward better stewardship practices.

### Survey Highlights

*Below are highlights from the seven sections of the survey. The full list of survey questions is on page 17.*

**Proxy Voting –** 100% of participants have an independent voting policy and their common practice is to utilize a proxy voting advisor.

**Engagement –** Only 57% of respondents received a passing grade; however, 67% of repeat respondents improved their engagement scores. Corporate engagement continues to be an area of improvement and increased focus for respondents.

**Stewardship Professionals –** Three quarters of participants have added professionals to their teams in the last five years, signaling the growing importance of stewardship activities.

**Disclosure –** Just over half of participants received a passing score, and 47% of repeat respondents received a lower score. We attribute this to a lack of standardization of firm level disclosure.

**Climate Initiatives –** 78% of participants have established guiding principles for climate risk assessment and 70% adhere to Task Force on Climate-related Financial Disclosures (TCFD) standards in their investment processes. Climate risk continues to be a focus for providers and the use of climate risk reporting standards is becoming increasingly common.

**Diversity, Equity, and Inclusion –** While most Sponsors (96%) have a DEI policy, only 74% received a passing score on our DEI section, largely due to a lack of tangible KPIs and programs beyond generalized policies.

**Sponsor Level Governance –** Although an overwhelming majority – 96% – of participants received a passing score, size determined relative performance. Smaller providers fared better, seemingly due to fewer legal proceedings.

## 2022 Annual Stewardship Survey Trends

This year's stewardship results revealed some emerging trends worth discussing, namely:

1. Unintended consequences: There was a noticeable decline in the level of manager disclosure and transparency, which likely reflected increased regulatory scrutiny.
2. Every vote matters: Proxy voting is extremely important, and those who have the power to cast votes carry great responsibility. Currently most of that power resides with passive fund managers, but that is starting to change.
3. Climate reporting standardization: ESG has come under fire for lack of standardization, but that is starting to change for climate risk reporting.

**Unintended Consequences**

There was a distinct change in tone as compared to previous years' responses. Companies that had once waxed poetic about their voting and engagement strategies seemed almost restrained, giving more guarded answers. What could cause such a noticeable change in a year? Regulatory action. Regulators in the US and abroad are cracking down on potential "greenwashing" by handing out fines to those asset managers who are found to be overselling their ESG credentials. This new wave of regulatory action has both positive and negative consequences. Greenwashing is likely to become less pervasive in the industry and managers will be more accurate in describing their ESG and stewardship capabilities, but lack of transparency could become a problem. Providers might become apprehensive about giving the full picture and risk the scrutiny of every detail by regulators. As a result of this curtailing of disclosure, some of the biggest managers in the space saw their grades decline this year.

**Every Vote Matters**

Proxy voting has always been one of the most important components of stewardship. The ETF Sponsor, rather than the individual investor, has traditionally had voting rights; however, proxy voting has become a hot topic among US policymakers. Several Republican senators have proposed a new bill, the Investor Democracy Is Expected (INDEX) Act, which aims to give investors, rather than ETF Providers, the power to determine how votes are cast. This act would require passive fund managers who hold more than 1% of a company's shares to collect investors' instructions and vote according to their wishes.[4] The INDEX Act is unlikely to pass with a democratic majority in Congress, but the idea of "pass-through" voting is becoming more popular.[5]

BlackRock, one of the world's largest asset managers and a long-time participant in our survey, has taken its own approach to pass-through voting, launching an initiative called "BlackRock Voting Choice," which allows certain institutional clients to "vote their own preferences" through a proprietary platform. This program currently applies to specific US institutional investors, including all US public pension clients and certain institutional investors in Canada and parts of the UK.[6]

In the meantime, the two major proxy voting advisory firms, ISS and Glass Lewis, remain firmly at the center of ETF providers' proxy voting processes. In our survey, 20 of 23, or 87%, of participants indicated that they use information from proxy voting advisors. Of that 20, all use ISS and/or Glass Lewis for proxy voting information. So many ETF providers using just two advisory firms begs the question: What is the true level of influence of these proxy voting advisory firms? Due to the outsized influence proxy voting advisory firms have on voting decisions that could affect long-term outcomes for corporations globally, it is incumbent upon the investing public to understand just how engrossed these firms are in the proxy voting process and how their opinions could help shape markets and potential outcomes.

**Climate Reporting Standardization**

The TCFD was created to improve and increase reporting of climate-related financial information. Its goal is to provide clear, comprehensive, high-quality information on the impacts of climate change.[7] It is our belief that the TCFD and its standards provide a pathway to successfully incorporating climate risks and opportunities into the investment process in a way that is focused on financial outcomes without agenda. We surveyed our respondents on the use of TCFD standards and found that 70% of managers incorporate those standards in their processes. The consolidation of and consensus on the use of TCFD standards shows a level of standardization in the ESG investing process as it pertains to climate considerations that has been sought by both proponents and opponents of the ESG investing movement. TCFD recommendations have been supported by jurisdictions around the world, including the United States, where the Securities Exchange Commission incorporated aspects of the TCFD framework for their proposed climate rules.[8] Additionally, the Principles for Responsible Investment incorporated questions related to the use of TCFD standards into their latest member questionnaire, using it as a potential metric for scoring. We expect the TCFD standards to keep picking up momentum as ESG investing continues to grow and climate remains a focus of core risk analysis.

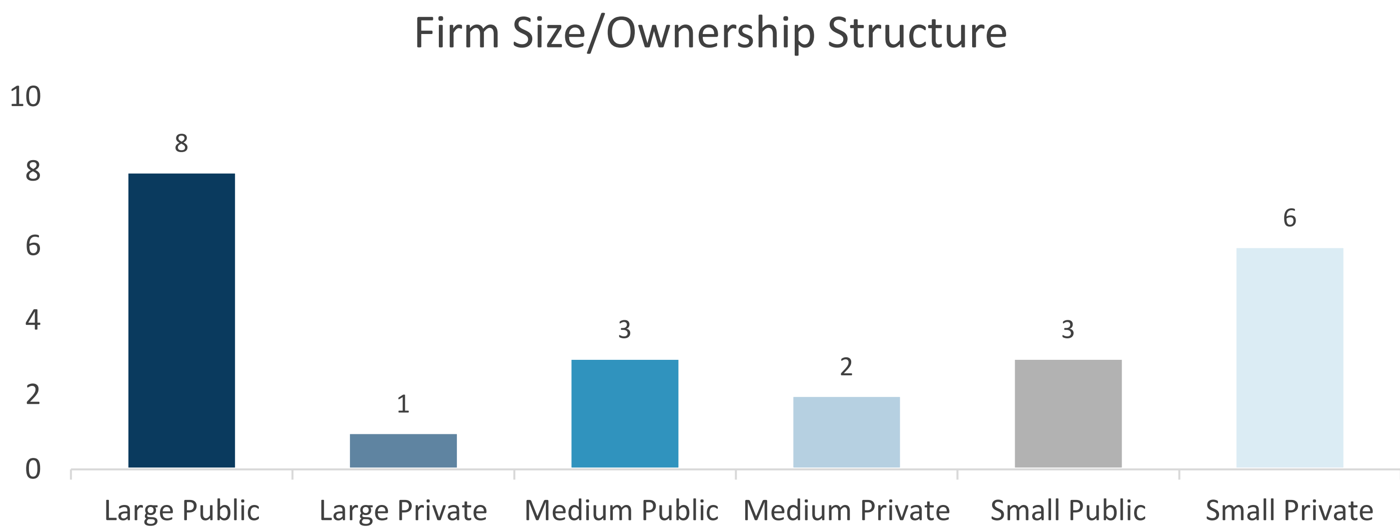
## 2022 Survey Participants

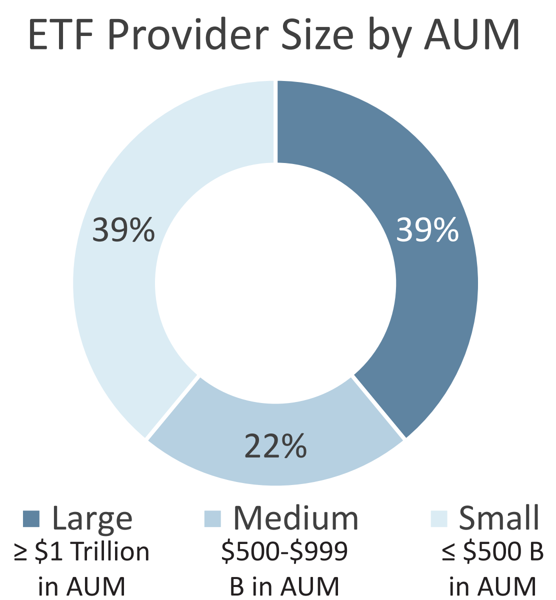
There were 23 participants in this year's survey, a record number. The largest ETF providers surveyed represent 7 of the 10 largest ETF providers in the US by AUM, and collectively our participants manage approximately $37 trillion in total assets and represent approximately 80% of global ETF AUM. We had 7 new participants and 15 repeat participants. Nine of our respondents have participated in our survey for the last four years.

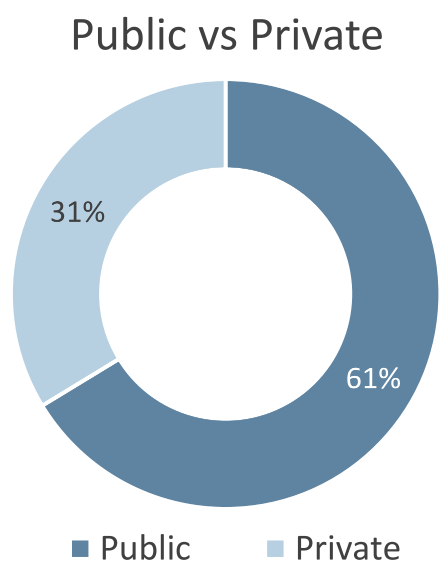
*Below is a list of the ETF providers who chose to participate this year, with special recognition to those who have participated for multiple years.*

| Firm Size | Firm Name | 2021 Participant | 2020 Participant |
|---|---|---|---|
| Large | J.P. Morgan | YES | YES |
| | BlackRock | YES | YES |
| | State Street | YES | YES |
| | Nuveen | YES | YES |
| | Franklin Templeton ★ | | |
| | Invesco | YES | YES |
| | Vanguard | | YES |
| | PIMCO | YES | YES |
| | DWS | YES | YES |
| Medium | Dimensional Fund Advisors | YES | |
| | Federated Hermes ★ | | |
| | Principal Global Investors ★ | | |
| | Charles Schwab | YES | YES |
| | IndexIQ | YES | |
| Small | ClearBridge Investments | YES | YES |
| | Janus Henderson | YES | YES |
| | KraneShares | YES | |
| | Hartford Funds ★ | | |
| | VanEck | YES | YES |
| | Global X | YES | |
| | Nationwide ★ | | |
| | Davis Advisors ★ | | |
| | Simplify Asset Management ★ | | |

★ New 2022 Participant




One notable difference in our process this year was to break out our providers into smaller peer groups based on total AUM. We believe this allowed for better comparison of the peer groups based on level of resources available. We categorized our providers into three peer groups:

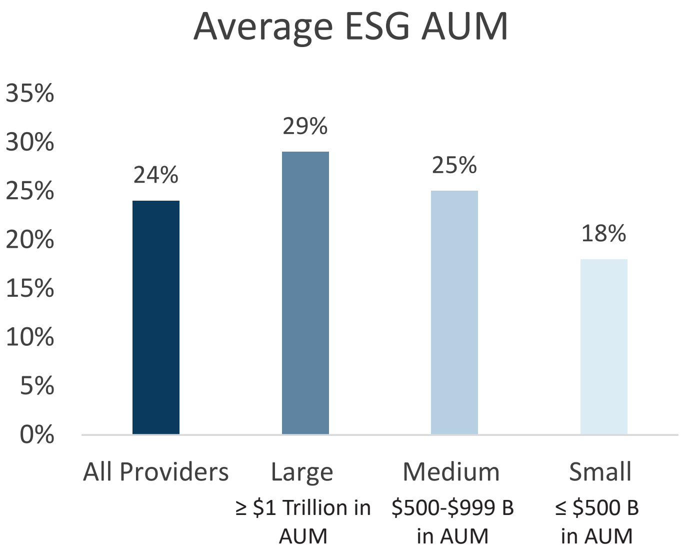
1) 39% were large providers, with at least $1 trillion in total AUM (as of the end of 2021).

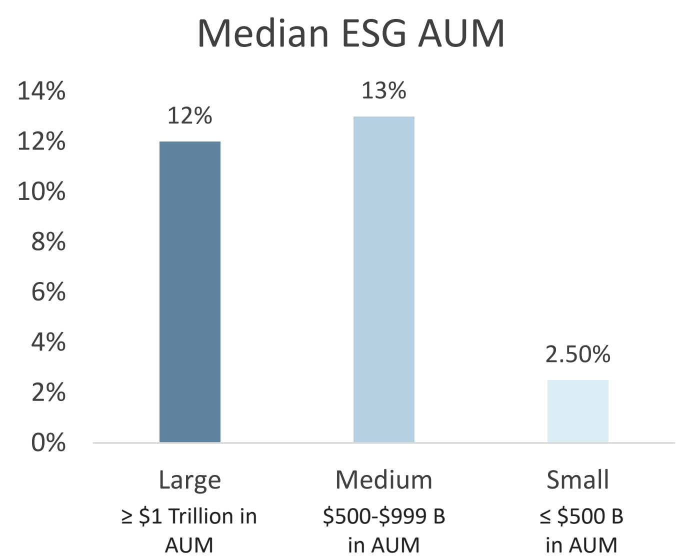
2) 22% were medium providers, with between $500 billion and $999 billion in total AUM.

3) 39% were small providers, with less than $500 billion in total AUM.

Additionally, providers were either privately owned (39%) or publicly held (61%). Large publicly held firms comprised 35% of survey participants, and small privately held firms represented 26% of our peer group.

The average ESG-mandated AUM of each provider was 24% of total firm AUM. Those in the large peer group had an average of 29% ESG-mandated AUM and a median of 12% AUM, followed closely by those in the medium category with an average of 25% ESG-mandated AUM and a median of 13%, then followed by the small peer group with an average of 18% ESG-mandated AUM and a median of 2.5%. Average AUM in ESG-mandated strategies was similar to that of last year in the largest category of providers. There was a very large difference between the amount of ESG-mandated AUM for medium and large providers, and there was significantly less ESG-mandated AUM among the smallest providers.




Additionally, being a signatory to the Principles for Responsible Investment (PRI) is seen as a signal of integrity and can serve as proof of credibility for managers of ESG investments. The majority, or 83% of our respondents, are signatories of the PRI. All large providers are signatories, 80% of medium providers are signatories, and 67% of small providers are signatories. We found this to be surprisingly low, given that all but one provider reported having ESG-mandated AUM.

## Survey Methodology

Our 2022 Sage Stewardship Survey covered seven areas of stewardship with a total of 69 questions. This year's survey included one new section, Sponsor Level Governance, which was added to provide insight into the internal governance practices of each sponsor. This year's survey consisted of a combination of "yes" or "no" questions and open-ended questions. As in past years, each question was given a maximum value of one to three points, and zero points were given for poor responses. Each section was tallied and rolled up to an overall score based on 61 possible points. Participants were given a letter grade of A, B, C, D, or F, based on their total scores.

| Letter Grade | Score (%) |
|---|---|
| A | ≥ 90% |
| B | ≥ 80% & < 90% |
| C | ≥ 70% & < 80% |
| D | ≥ 60% & < 70% |
| F | < 60% |

## Survey Results

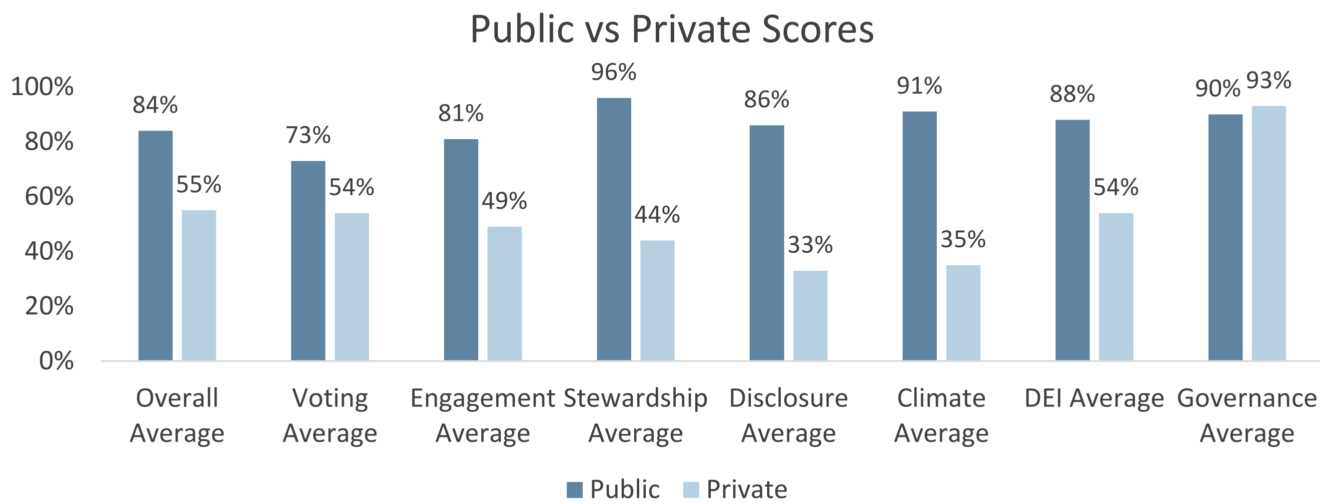
We are pleased to reveal that this year 70% of participants received an overall passing score of C or better, and 73% of repeat participants received a passing score this year, demonstrating continued improvement. The number of providers who received an overall score of A grew this year from four to seven, and six of those seven were repeat respondents.

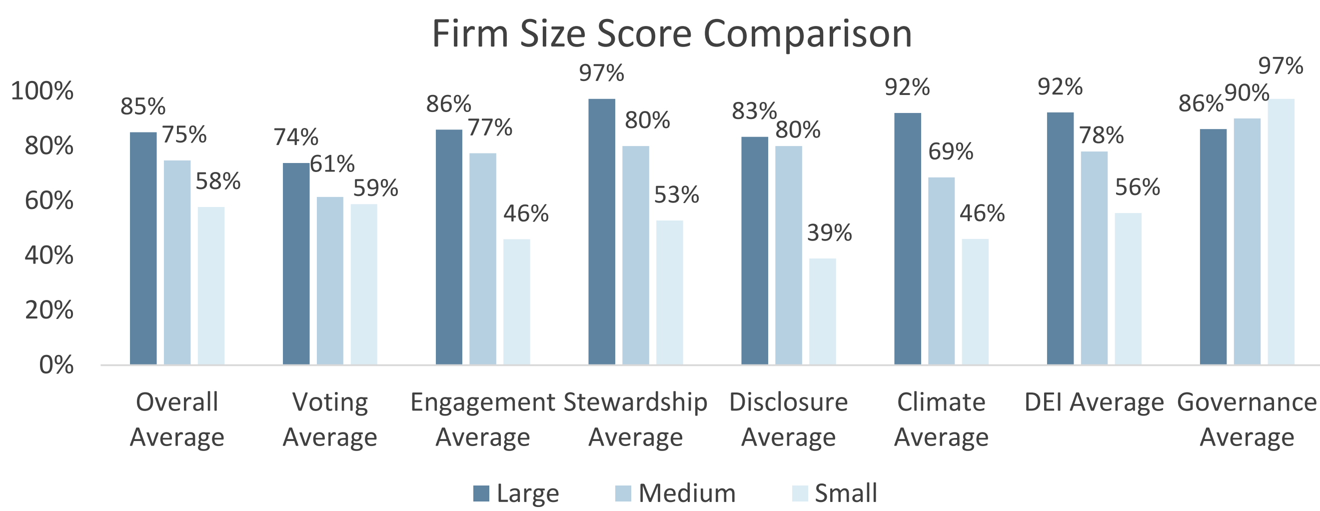
There does seem to be a correlation between size and ownership structure and overall score potential. Large public and large private firms fared well, with an overall average score of B and A, respectively. The divide between public and private firms became more noticeable in the smaller categories, with medium public providers scoring an average of C and medium private providers scoring an average of D. The most significant difference was between small public and small private firms: Small public firms outperformed small private providers by a vast margin. Small public firms averaged an overall score of B while small private firms scored an average of F. Small public firms were a clear standout in terms of performance, considering that their average score was on par with that of large public firms, which further affirms our belief that intention can win over size.

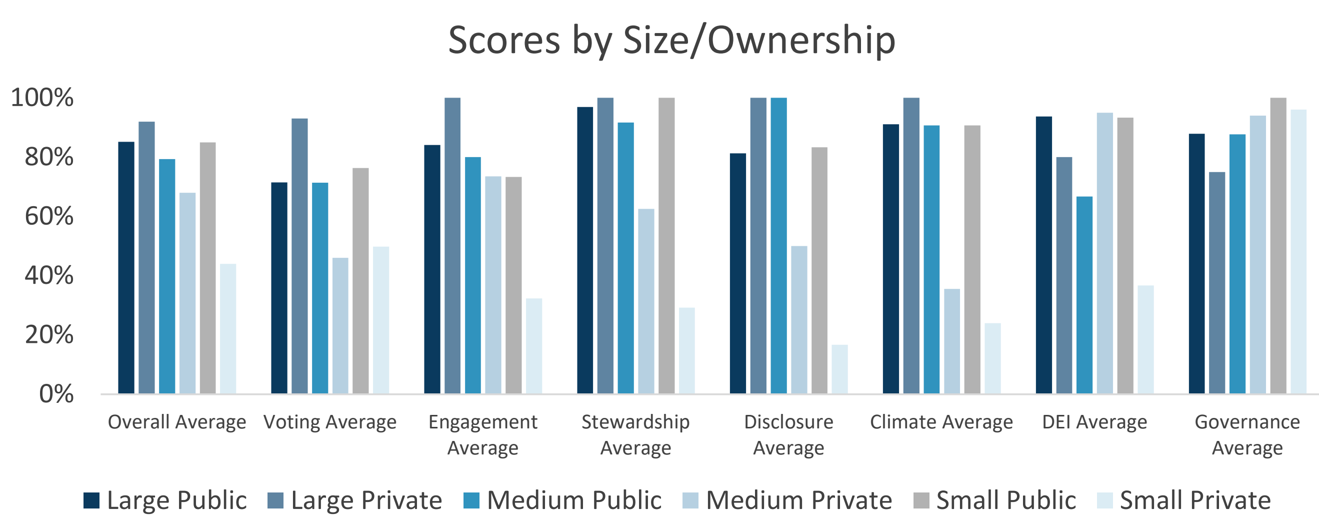
# 2022 ETF Stewardship Survey Results

| 2022 Participants | Overall 2022 Score | 2022 Voting Score | 2022 Engagement Score | 2022 Stewardship Score | 2022 Disclosure Score | 2022 Climate Score | 2022 DEI Score | 2022 Sponsor Governance Score |
|---|---|---|---|---|---|---|---|---|
| Large Public 1 | A | C | A | A | A | A | A | B |
| Large Public 2 | A | C | A | A | A | A | A | B |
| Large Public 3 | A | C | A | A | A | A | A | B |
| Large Public 4 | A | C | A | A | A | A | B | A |
| Large Public 5 | B | B | D | A | A | A | A | A |
| Large Public 6 | B | C | A | A | A | B | A | D |
| Large Public 7 | C | F | A | A | F | B | A | B |
| Large Public 8 | F | C | F | C | F | F | C | B |
| Medium Public 1 | C | F | C | A | A | B | B | A |
| Medium Public 2 | B | C | A | A | A | A | F | B |
| Medium Public 3 | C | B | D | C | A | B | C | C |
| Small Public 1 | A | C | A | A | A | B | A | A |
| Small Public 2 | A | A | B | A | A | A | A | A |
| Small Public 3 | C | F | F | A | F | B | A | A |
| Large Private 1 | A | A | A | A | A | A | B | C |
| Medium Private 1 | F | F | F | F | F | F | A | B |
| Medium Private 2 | B | C | A | A | F | C | A | A |
| Small Private 1 | F | F | D | F | F | F | F | A |
| Small Private 2 | F | F | F | F | F | F | A | A |
| Small Private 3 | C | C | B | A | F | B | F | B |
| Small Private 4 | F | F | F | F | F | F | F | A |
| Small Private 5 | F | F | F | F | F | F | F | B |
| Small Private 6 | F | F | F | F | F | F | F | A |

Below are score averages for each size group and ownership structure. In most categories, larger size and public ownership structure translated into higher average scores, with the notable exception of governance, where the opposite was true. We will expand upon this in the Sponsor Governance section of this report.



# Proxy Voting Practices

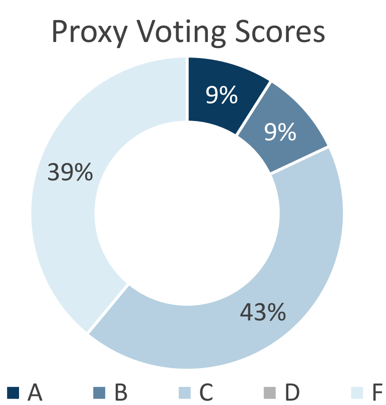
Voting is a key tenet of stewardship and active ownership. Voting has the power to steer company management and strategy, help determine the makeup of boards of directors, and usher in policies that help shareholders gain more insight into the operations of the organizations in which they are invested. Voting can improve shareholder value, and therefore remains an exceedingly important tool for investors.

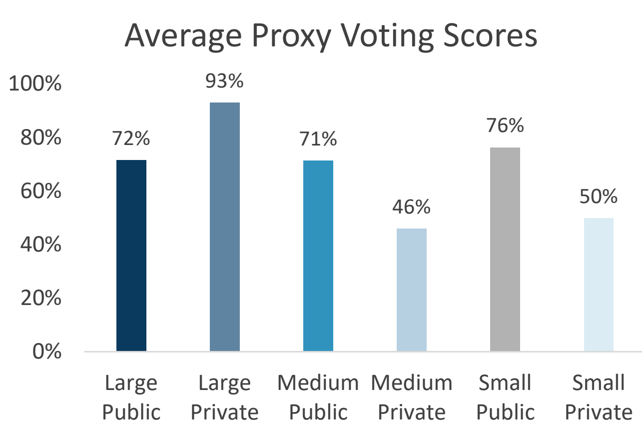
**Proxy Voting Practice Process Improvements**

This year we added several questions to the Proxy Voting Practices section to reveal information about each provider's use of country-specific stewardship codes, as well as voting decisions on shareholder-led proposals. We also inquired about the primary motivation for integrating ESG into the investment process.

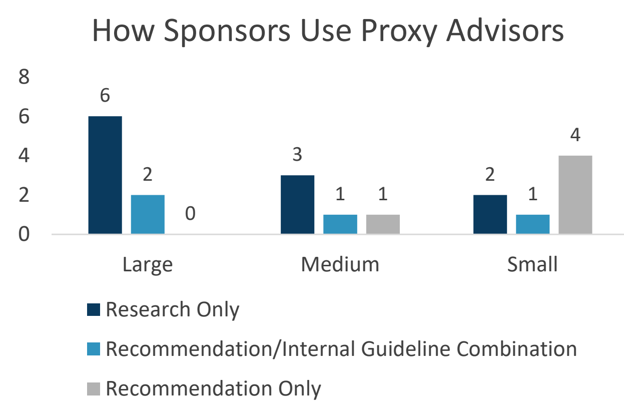
**Proxy Voting Practices Results**

This year 61% of the participants received a passing score on the Proxy Voting Practices section, down from 71% in 2021. This decline in passing rate can be attributed to both a larger group of participants and weakness in a few key areas. It should be noted that 73% of our repeat respondents received a passing score this year.

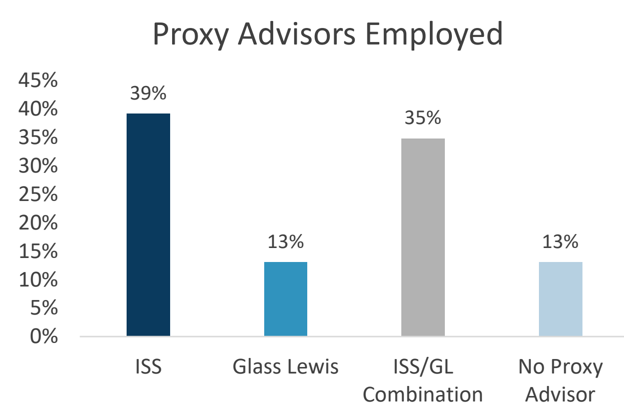



All ETF providers had either an independent proxy voting policy or a formal policy regarding the delegation of voting decisions to proxy voting advisory firms. Most providers (87%) use a proxy voting advisor in some capacity to aid in the decision-making portion of the proxy voting process; 55% use advisory firms to exclusively inform their research processes; 20% use recommendations from the advisory firms but also use their own guidelines; and 25% rely solely on the recommendations of the advisory firms. Size was a determining factor in this difference. Smaller firms were most likely to use recommendations from advisory firms rather than in-house research to determine voting decisions. Smaller firms often have fewer resources at their disposal and a greater potential need to outsource, so this is somewhat unsurprising.




As mentioned, ISS and Glass Lewis dominate the market for proxy advisory services, with ISS at 74% market share.




In our view, best practice would be to either conduct all proxy research in-house or use proxy advisory firms purely as research vehicles rather than a recommendation source, given the tremendous influence that these firms have on current proxy voting decisions. To provide some background, proxy advisory firms give recommendations for how to vote proxies for companies within ETF Provider portfolios, and ETF Providers can choose to vote in line with the recommendations or simply use them as research data points in their voting decision process.

We also assessed non-routine voting activities and the exercise of direct voting rights. (Non-routine decisions include an auditor change, company name change, etc. They are important because these votes change company strategy and determine important shareholder value-changing decisions.) In total, 74% of providers affirmed that they assess all non-routine voting activities, and only 26% reported exercising voting rights for all portfolio companies; 59% of those providers who did not report exercising voting rights for all portfolio companies had reasons for not doing so that we believed were sufficient to regain two points. It is our belief that ownership rights should be utilized and votes cast for all portfolio companies.

Votes against management were assessed, and we found that only 30% of providers voted against management more than 10% of the time. This percentage has diminished greatly from our 2021 and 2020 surveys, and we largely attribute this change to a decline in manager transparency. Unfortunately, several respondents declined to answer the question by either not giving a percentage, providing their overall voting record instead, or keeping the information confidential. In fact, only 52% of respondents provided a percentage at all.

In this section, we also analyzed how ESG factors affect the voting practices of providers. Of our participants, 78% reported that ESG-related factors impact voting behavior and 65% have an ESG-specific section in their proxy voting guidelines. However, 93% of repeat respondents reported incorporating ESG-related factors into their voting decisions, a far greater percentage than that reported by the broader peer group.

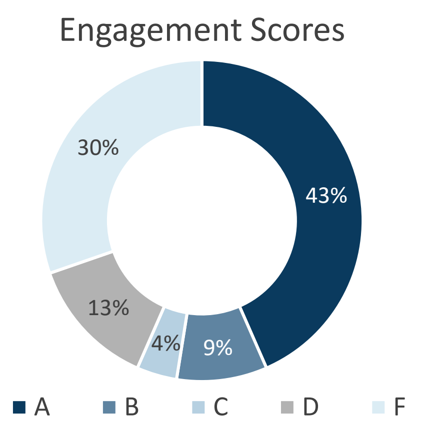
Lastly, we surveyed respondents on their use of securities lending and found that 87% of providers participate in securities lending. Although we understand that income from securities lending can be used to supplement returns, it is our belief that securities lending also comes with risk, as ownership rights are temporarily suspended for the owners. If securities aren't recalled in time to cast votes, the risk is that ownership rights will be forfeited.

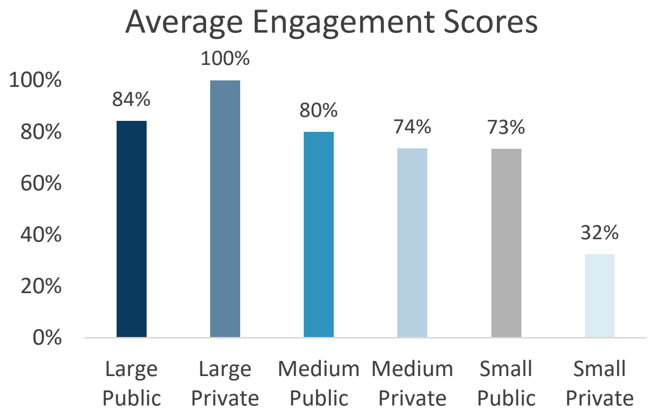
# Engagement

Engagement is the other core tenet of stewardship and a complement to the voting process, so we emphasize both equally in terms of questions and points awarded. Our Engagement section has evolved over the years, culminating in a comprehensive set of questions aimed at discovering the nature of each provider's practices.

**Engagement Process Improvements**
Our 2022 survey included a new set of questions that focused on engagement versus voting, including whether participants believed it was more effective to engage with or vote against company management. We also wanted to know if providers were more focused on monitoring portfolio companies and their actions or having two-way dialogues focused on driving positive change. We inquired about whether engagement activities were outsourced and whether they were documented and made available to ETF investors. Lastly, we included a request for examples of meaningful engagements, which prior to this year was part of our disclosure section.

**Engagement Results**
Our engagement scores were a mixed bag, with 57% of providers receiving a passing grade. In fact, while 43% of providers received a score of A, 30% of providers received a score of F, creating somewhat of an inverted bell curve distribution. Although size does seem to play a factor in engagement scores, some of our highest engagement scores were achieved by smaller managers. Most of the providers that received a score of F on the Engagement section did not have an engagement program or fully deferred to subadvisors for their engagement processes. Although this is concerning, we are hopeful that as stewardship continues to be at the forefront of investor focus and demand, all providers will begin to formalize and integrate their engagement strategies. On a positive note, of the 15 repeat survey respondents, 67% saw an improvement in their score, again providing evidence of the impactful nature of our stewardship work.




Most providers (74%) had formal engagement policies, with even more (83%) providing responses about how their engagement practices were carried out. We view this as a missed opportunity for some providers and believe that best practice would be to formalize policies. Engagement activities were, for the most part, managed internally (78%). Although it was our hope that each provider would detail their approach to voting versus engagement, only 70% provided reasons for practicing both methods. We found that 43% of our respondents did monitor engagements, 61% participated in two-way dialogue engagements that sought to drive positive change, 65% had company-specific engagements, and 43% considered thematic goals when engaging. Although this provided greater insight into engagement methods, only 65% of providers gave responses. Although only 65% of providers explained what types of information were gathered during engagements, nearly all the respondents that reported practicing engagement gave some tangible evidence of their practices.

Our survey also posed a line of questions regarding engagement success, metrics for success, and post-engagement time frames, and asked for explanations for all. Of the providers that had a formal engagement program, 75% had metrics for engagement success, which was in line with last year's survey results. Additionally, 35% of providers cited having a post-engagement time frame for success, or proof of measurable changes at the portfolio company level attributable to engagement. Although this percentage seems small, it is a noticeable improvement from our survey last year, when only one provider noted having time frames for success. Best practice would be to outline overarching metrics for success, such as a step-by-step process for initial engagement, expected company management reactions to those engagement efforts, and subsequent details on changes made to remedy investor concerns and follow-up by providers. And although we understand that each engagement is unique, we believe there should be a generalized time frame in which change is expected.

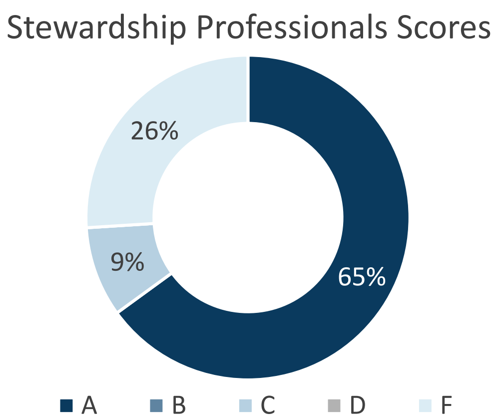
Escalation strategies are a crucial part of engagement and should be a component of any engagement process. It is through escalation that investors can increase the intensity of their engagement efforts and decide to either continue toward a successful outcome or exit an investment due to an ongoing lack of momentum. Overall, 57% of our respondents answered affirmatively to having some sort of escalation strategy, and on an encouraging note, 75% of providers with a formal engagement strategy had an escalation strategy.

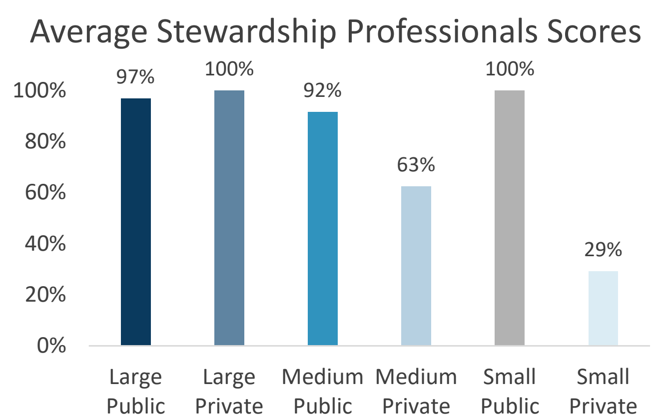
Engagement examples help ETF investors understand the types of discussions providers are having with company management and how those discussions are culminating in measurable changes and successful outcomes. The majority (65%) of providers gave engagement examples with the level of detail and outcome reporting that satisfied our best practice benchmark. Again, when looking at the data through the lens of providers with in-depth engagement strategies, 94% of those respondents gave thorough examples of engagements and their outcomes. This represents an improvement from last year and is likely due to increased investor demand for transparency surrounding engagement practices. We are pleased that providers seem to be hearing the calls for more information regarding engagement, and we will continue to advocate for increased transparency and outcome reporting from all ETF providers.

# Stewardship Professionals

> A company is only as good as the people it keeps."
>
> *Mary Kay Ash, founder of Mary Kay cosmetics*

**Stewardship Professionals Process Improvements**
From a policy perspective, we wanted to determine if stewardship had been formalized at the company level through a formal investment stewardship policy, as well as gauge the maintenance of and compliance with the policy. Second, we added a question regarding training for professionals aimed at keeping them informed of the most pertinent topics facing stewardship and ESG-related practices.




**Stewardship Professionals Results**
The majority (74%) of our providers received a passing score for this section, and 65% received a score of A. Again, size seemed to play a role, as did ownership structure. Companies with more resources and public ownership fared better, while those that were smaller and had fewer resources and private ownership lost critical points needed to achieve a high score. Stewardship policies were common, with 78% of providers reporting having one. Stewardship evaluation teams were also widespread; 78% of providers have a team in place, and 74% of providers have added professionals to the team over the last five years. In our opinion, stewardship teams should be a part of every provider's employee base due to the sheer number of votes and engagements that take place each year.

Our last focus was on evaluating the training resources available to stewardship and investment personnel who are involved in the stewardship process. We found that 74% of our respondents provided training to professionals. Although the type of training varied by firm, we were satisfied to see that resources were being allocated to continuing education.

# Disclosure

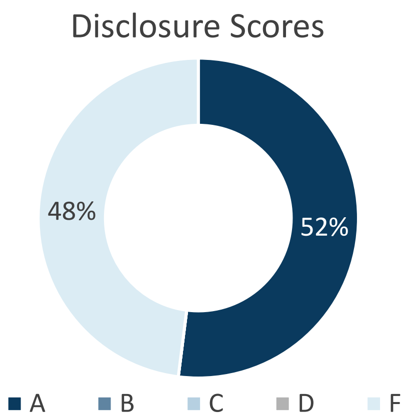
Disclosure remains one of the most important aspects of stewardship, and transparency is essential to any successful investment management process. Therefore, we have included a Disclosure section in our survey for several years and continue to build upon the knowledge and insights we have gained.

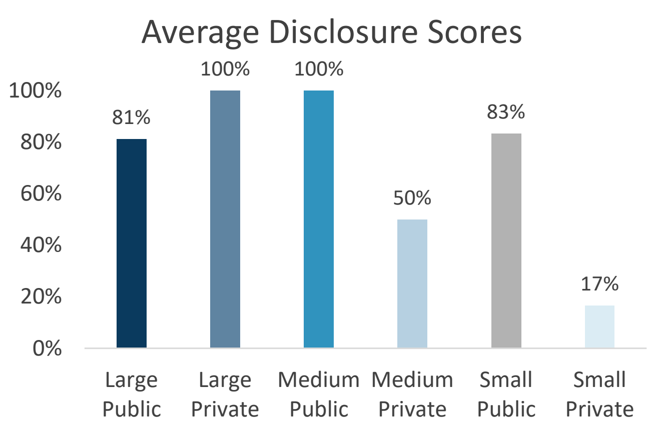
**Disclosure Process Improvements**
This year we included questions regarding corporate reporting frameworks that providers subscribe to for their firmwide disclosures. We provided examples, including the Sustainability Accounting Standards Board (SASB), Taskforce for Climate-related Financial Disclosure (TCFD), Global Reporting Initiative (GRI), etc. Interestingly, we found that 52% of our respondents were already utilizing established frameworks for reporting or are considering such frameworks. The most commonly used reporting frameworks were SASB and TCFD. Six providers reported using SASB standards and 11 providers reported using TCFD standards. Others that were named were GRI, UK Stewardship Code signatory, Climate Disclosure Project (CDP), and United Nations Sustainable Development Goals (SDGs). The remaining question in the Disclosure section involved disclosure of voting records.

This year we specifically requested that providers attach their voting records with their completed survey questionnaires upon submission. Disappointingly, only 78% complied. We believe that making voting records easily available to investors maintains trust between the ETF investor and the sponsor and is best practice. To that end, in future surveys we will be requesting summarized versions of voting records in order to provide some clarity for the vast number of voting decisions made by our survey respondents each year.

**Disclosure Results**

We are concerned about the apparent decline in our respondents' overall transparency and disclosure scores as a result of a lack of standardization of firm-wide disclosures. As regulatory bodies scrutinize sustainability practices further, it would be prudent for providers to utilize a standardized reporting framework. Only 52% of our respondents received a passing grade for this section, but more concerningly, 47% of repeat respondents received a lower score as compared to last year.



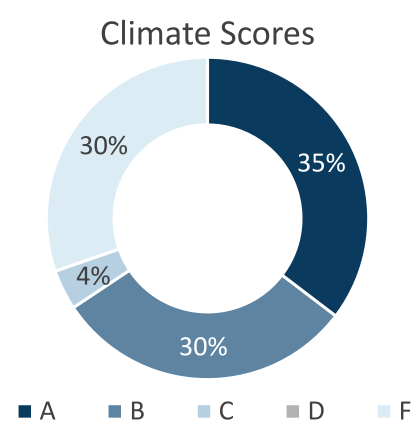

# Climate

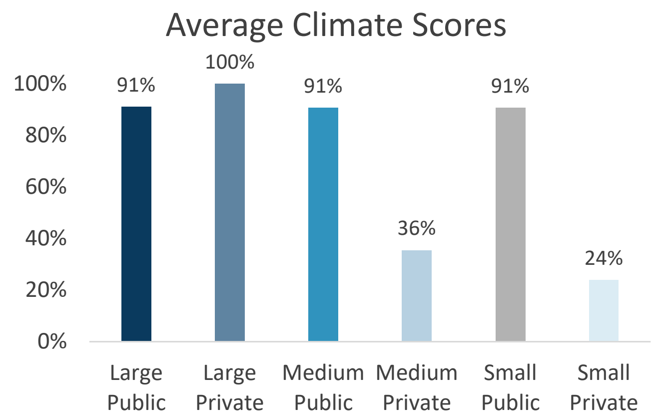
According to the Intergovernmental Panel on Climate Change (IPCC), warming of the atmosphere caused by humans is undeniable and rapid changes to our planet have already occurred. The latest report also explains that many of the emissions we have already created will affect the planet for millennia, and we must work to reduce further emissions now. "Pathways limiting global warming to 1.5°C with no or limited overshoot would require rapid and far-reaching transitions in energy, land, urban and infrastructure (including transport and buildings), and industrial systems…" The panel suggested that investment in transitional opportunities should be made immediately.[9]

Considerations of climate change within the investment process have become more commonplace in the asset management industry, and in fact many of the respondents to our survey cited climate change as one of the greatest risks facing not just our planet, but also our investments. Therefore, for the last several years we have analyzed providers' policies surrounding climate and how they impact investment and stewardship activities.

**Climate Process Improvements**

This year we added a focus on how climate change is considered in each provider's process and how carbon risk is measured. Additionally, we included the consideration of the use of TCFD standards and recommendations in investment processes and asked our respondents to provide their climate-specific voting records. For our climate section, 70% of providers received a passing score this year, an improvement from last year, when just over half of providers received a passing score. We see this improvement as a positive sign that providers are taking all risks into consideration, including climate change risks, when managing their investments and stewardship responsibilities. Once again, size seemed to determine Climate section scores due to the lack of incorporation of TCFD standards, the absence of climate-related engagement strategies, and deficient monitoring of portfolio companies' oversight of climate-related risks and opportunities.






**Climate Results**
To understand each provider's climate strategies, we first inquired about each sponsor's guiding principles for climate risk management. We found that 78% of providers had some sort of guiding principle on climate risk, a slight improvement from last year. Next, we delved deeper into how climate risk assessment is incorporated into the provider's process and how carbon risk is measured. While 78% of providers also gave us detailed information on their incorporation of climate change risk analysis and carbon risk analysis, we would ideally like to see all providers incorporate this risk analysis into their practices.

Climate change poses a substantial threat to investments through physical and transition risks, Therefore, we believe there is a very tangible investment risk that should be examined. The TCFD was created to improve and increase reporting of climate-related financial information. Its goal is to provide clear, comprehensive, high-quality information on the impacts of climate change.[7] It is our feeling that the TCFD and its standards provide a pathway to successfully incorporate climate risks and opportunities into the investment process in a way that is focused on financial outcomes without agenda. While only 70% of managers incorporate TCFD standards in their processes, we are encouraged by the fact that most managers are already incorporating the standards in some way. We would like to see greater adoption of these standards and will be continuing to monitor their use.

As a separate study, we compared the list of providers who identified as signatories of the Net Zero Asset Managers (NZAM) initiative against the list of providers who use the TCFD standards in their process and found that 88% of NZAM signatory managers use the TCFD standards. While we would expect a 100% match between these two practices, it is encouraging that most managers consider both organizational frameworks.

Climate-specific engagement efforts are another key piece of climate-related strategies, and 70% of our respondents answered with details outlining their engagement processes as they relate to climate. However, when narrowing our lens to include only those providers with an overall engagement strategy, 94% of those providers had climate-specific engagement efforts.

The last questions in our Climate section were focused on portfolio company oversight of climate risks and voting history in relation to portfolio level company disclosure on climate change risks and how they are managed. The respondents that monitor portfolio level oversight represented 70% of the peer group, and those that indicated voting in favor of proposals that pertained to portfolio level company disclosure and climate change risks represented 52% of providers. Although attachment of climate-related voting records was not a scored criterion this year, we did note that only 39% provided such information. In the future we will likely score this factor, and best practice would be to give either the exact voting record on climate-related proposals or some level of summary data.

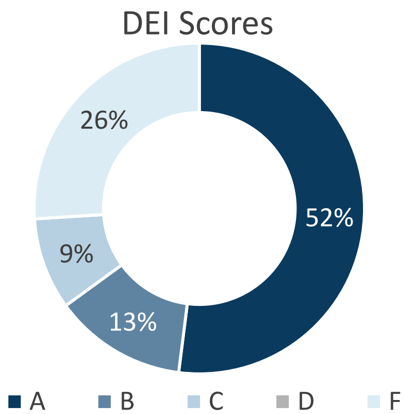
## Diversity, Equity, and Inclusion

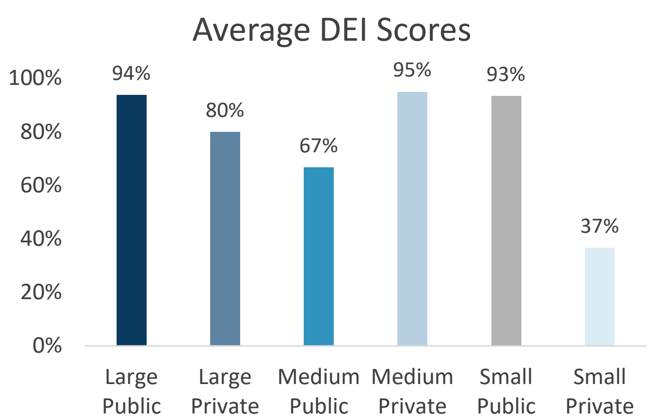
Diversity is a driver of innovation and financial performance, and there is a statistically significant relationship between diversity and innovation.[10] Although Diversity, Equity, and Inclusion (DEI) initiatives are common in US corporations, they are found to be somewhat ineffective, as illustrated by the prevalence of diversity or inclusion lawsuits.[11]

**DEI Process Improvements**
In an effort to strengthen our analysis of each provider's DEI initiatives, we added several questions that went beyond policies and dug into key performance indicators (KPIs) to prove that policy initiatives are actionable and demonstrable. Additionally, we incorporated questions regarding each provider's oversight of portfolio companies DEI initiatives and statistics to understand how this information feeds into the stewardship practices of all providers.

**DEI Results**
In total, 74% of our respondents received a passing score on our DEI section. This is a large decline from last

year's results, when 88% of providers not only passed but received a score of A. The lower scores are a direct result of the greater intensity of our questions about tangible KPIs and programs beyond generalized policies.

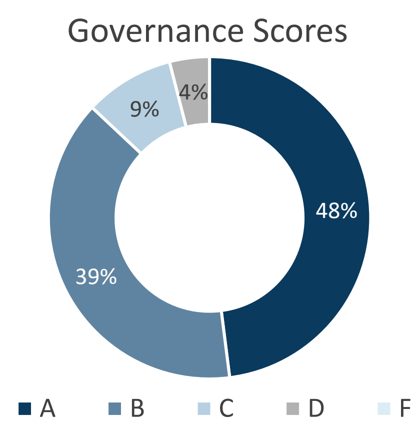


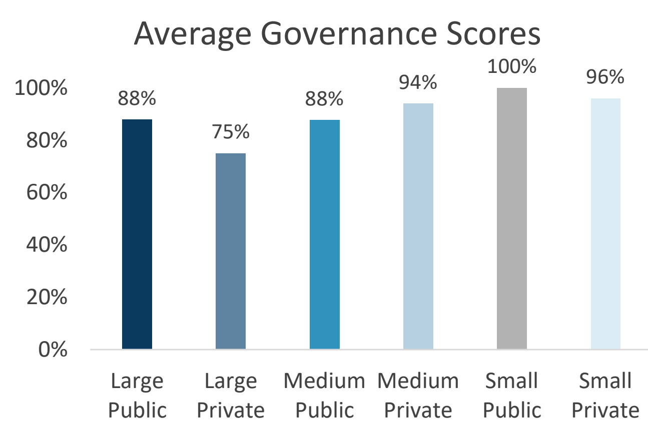




Our survey questions first focused on each respondent's DEI policies and monitoring/reporting on the demographic information of employees. Most providers excelled in this area, with 96% of respondents having a stated DEI policy and 96% stating that they monitor and report on this information. From there, we pushed further and asked about plans and policies designed to promote equity at all levels of their companies, and specifically at the senior leadership and C-suite levels. Overall, 87% of providers responded that they had plans and policies in place to promote equity at all levels, but only 78% indicated having a plan in place for promotion of equity at the upper levels of the company. To confirm our findings, we asked providers if they had KPIs for tracking DEI initiatives and, if so, if they were available to external parties. Once again, only 74% of providers indicated having KPIs related to DEI goals, and an even smaller number (48%) made those KPIs available to external parties. On a more positive note, 87% of providers have mentorship programs for either women, minorities, or both; however, only 65% have a formal pay parity policy in place despite the focus on mentorship. Lastly, regarding our question about DEI tracking at portfolio companies, we found that only 57% of providers track this level of information at that level. DEI is a work in progress, and we hope to see measurable changes over time.

## Sponsor Level Governance

The newest section of our survey is the Sponsor Level Governance section. As suggested by the CFA Institute, "Weak corporate governance is a common thread found in many company failures."[12] We believe companies must be well managed internally to manage their externally facing activities, including investing and stewardship. Therefore, we chose to consider the governance practices of our participants to further our due diligence process beyond stewardship activities alone. In doing so, we learned a great deal about how each of our respondents are governed and structured and how they operate around legal and regulatory issues. We are happy to report that 96% of our respondents received a passing score in this section.



Our governance questions had several dimensions focused on various aspects of the governance sphere. The first order of business was understanding compensation and remuneration policies for executives; 87% of providers were willing to give details on compensation and remuneration policies for their firms, but not all provided these details for their top executives. We plan to revise this question for future surveys, making it even more specific, and hope to have greater transparency around the remuneration practices of top executives.

We then turned our attention to other policies, including lobbying and political donations, whistleblower, ethics and codes of conduct, and sexual harassment. Most providers had all the above policies; 100% had some sort of lobbying and donation policy, 96% had a specific whistleblower policy, 100% had ethics and codes of conduct policies, and 100% had sexual harassment policies.

Board structure varied considerably among the providers; 19 of 23 providers reported having a board. Regarding board tenure, results were mixed, with the average tenure ranging from 19 months to 25 years. Additionally, 14 providers revealed either minority or gender representation on their boards and 19 providers provided data on the level of board independence.

Somewhat remarkably, the size and ownership structure of the firms did have an impact on governance scores. Our results showed that smaller, privately held firms outperformed their large and public counterparts. We can attribute this result directly to legal proceedings, as larger and publicly held providers had a significantly greater likelihood of involvement in ongoing legal proceedings. In fact, 39% of all providers and 67% of large providers had involvement in legal proceedings. Although we are dismayed at the number of ongoing legal proceedings involving several providers, overall we are pleased with the results of the Governance section and the focus providers seem to place on governance in general.

## Sources:


1. Flood, Syl. "Global Flows H1 2022: A Moderate Pullback from Fixed-Income." Morningstar Research. July 22, 2022.
2. Gordon, Jamie. "Passive's ownership of S&P 500 doubles in seven years." ETFStream.com. June 08, 2022.
3. Chen, Max. "ETF Industry Is Positioning to Break $10 Trillion in AUM." VettaFi. December 27, 2021.
4. Foster, Lauren. "Proposed Legislation Promises to Empower Investors. What to Know." Barron's. June 14, 2022.
5. Nadig, Dave. "The INDEX Act: The Next ESG Battle Is For Your Vote." VettaFi. August 5, 2022.
6. Boss, Sandy,et al. "It's all about choice." BlackRock. June, 2022.
7. Task Force on Climate-related Financial Disclosures website.
8. "Climate Disclosure Convergence: TCFD, SEC, and ISSB." TCFD. May 2022.
9. Allen, Myles, et al. "Summary for Policymakers." IPCC. 2018.
10. Lorenzo, Rocio & Martin Reeves. "How and Where Diversity Drives Financial Performance." Harvard Business Review. January 30, 2018.
11. Anwar, Mohammad. "The Future of Diversity and Inclusion in Corporate America." Forbes. May 5, 2022.
12. "Introduction to Corporate Governance and Other ESG Considerations." CFA Institute. 2022.

# 2022 ETF Stewardship Survey Questions

The 2022 Sage Stewardship Survey consisted of seven sections:

Prologue: General Sponsor Information – 1 point
Section I: Proxy Voting Practices - 14 points
Section II: Engagement – 15 points
Section III: Stewardship Professionals – 4 points
Section IV: Disclosure – 2 points
Section V: Climate Initiatives - 7 points
Section VI: Diversity, Equity, and Inclusion – 10 points
Section VII: Sponsor Level Governance – 8 points

### General ETF Sponsor Information

1) Is (the Sponsor) a publicly or privately held entity?
2) What is the (the Sponsor)'s ownership structure? What is the percentage of the firm ownership held internally versus externally?
3) What was (the Sponsor)'s total combined AUM as of FY 2021?
4) What percentage of AUM represents ETFs, mutual funds, and SMAs?
5) What percentage of (the Sponsor)'s total AUM has an ESG mandate?
6) Do any of (the Sponsor)'s funds qualify as thematic? If so, what is the thematic focus of these funds?
7) Is (the Sponsor) a member of the UNPRI? If so, please list the year the firm first became a PRI signatory.
8) What is (the Sponsor)'s most recent PRI Strategy and Governance firm score?
9) Is (the Sponsor) a member of the Net Zero Asset Managers Initiative? If so, what ETFs (if any) are aligned with the initiative? (i.e., aligned with net zero emissions by 2050 or sooner).
10) Does (the Sponsor) have an ESG score or rating? If yes, from which organization(s) (e.g., MSCI, Sustainalytics, Arabesque, ISS, Vigeo Eiris)? Does (the Sponsor) consult with ESG ratings organizations for score improvement?
11) Does (the Sponsor) contract with any external consultant or provider for ESG monitoring or integration services?

### Proxy Voting Practices

1) Does (the Sponsor) have independent proxy voting policies? If so, please provide the stated policies.
2) Does (the Sponsor) formally retain or engage with a proxy voting advisor?
   a. If yes, in what capacity does (the Sponsor) utilize information or guidance from the proxy advisor's company? (e.g., research, voting recommendations, statistical surveys)
   b. If the information is used for voting recommendations, does (the Sponsor) align in-house voting policies with the recommendations? Please provide an example.
3) Are voting guidelines consistent across all strategies, asset categories, and geographic regions? Please provide a brief explanation.
4) Do varying countries' rules and regulations regarding shareholder proposals influence or affect (the Sponsor)'s voting behavior? (e.g., in Europe versus the United States). Please provide a brief explanation.
5) Does (the Sponsor) leverage country-specific stewardship codes in the investment process? If so, which ones?
6) Does (the Sponsor) assess all non-routine voting activities? Please provide a brief explanation of this process.
7) How many ETF portfolio companies does (the Sponsor) exercise direct voting rights for? How does the sponsor choose which portfolio companies to exercise proxy voting for? Are there thresholds, i.e., a proxy vote requires the company to have a minimum portfolio weight?
8) In the past year, what percent of total votes has (the Sponsor) made in favor of portfolio company management positions?
9) If (the Sponsor) voted in favor of shareholder-led proposals, please identify the nature of the proposals or topic of concern.
10) Does (the Sponsor) view a negative vote as a way to effect change in a portfolio company? Please provide a brief explanation.
11) How does (the Sponsor) consider ESG factors when voting? What was the primary motivation initially for integrating ESG into the product's investment process? Are ESG issues considered as distinct financial risks, opportunities in addition to traditional financial analysis?
12) Does (the Sponsor) engage in securities lending? If so, what percentage of portfolio holdings will (the Sponsor) lend?

### Engagement

1) Does (the Sponsor) have a formal corporate engagement strategy? If so, please attach.
2) How often does (the Sponsor) engage with ETF portfolio companies? What percentage of portfolio companies are engaged with annually?
3) Are engagements formalized monitoring engagements (scheduled, information gathering) or two-way

# 2022 ETF Stewardship Survey Questions

dialogue engagements (i.e. looking to constructively effect change with outcomes)?
Are engagements company specific or thematic in nature (i.e., sector/industry wide topic evaluations on which (the Sponsor) engages with all companies in that sector/industry)?
4) Does (the Sponsor) outsource any engagement activities?
5) What is the relationship between company engagement and proxy voting?
  a. When is engagement exercised versus voting, and how often is each practice applied?
  b. What are (the Sponsor)'s views on engagement with company management versus voting against company management?
  c. Is engagement ever used in lieu of a vote against management proposals? If so, how frequently?
6) What information does (the Sponsor) seek from engagement with portfolio companies? (e.g., operating data, ESG data, general information gathering, policy voting intentions, executive compensation policies).
7) Are there industries where engagements are of greater importance than others? If so, please explain.
8) Is (the Sponsor) more or less likely to engage with companies that represent a higher portfolio weight? Please explain.
9) What group or department at (the Sponsor) is responsible for corporate engagement activities?
10) After engaging directly with a portfolio company, what is the time frame that (the Sponsor) will allow portfolio companies to effect change? Are the activities chronicled and available to ETF investors? If there is no specific time frame, please provide an explanation.
11) How does (the Sponsor) determine if an engagement was successful? How are outcomes measured and are they made available to ETF investors?
12) Please include examples of meaningful engagements with portfolio companies and the policies addressed.
  a. Please provide examples of measurable changes that have occurred as a result of direct engagement(s) with companies.
13) Is there a post-engagement escalation strategy if it is determined that necessary changes have not been made by the portfolio company?
14) Does (the Sponsor) lead or participate in collaborative engagements through industry organizations (e.g., Ceres, PRI, USSIF, Climate Action 100+)? If so, please provide specific examples of collaborative engagements.
15) Does (the Sponsor) engage with independent or governmental policymakers or standard setters? If so, please provide examples of these engagements.

### Stewardship Professionals

1) Does (the Sponsor) have a formal investment stewardship policy? Is it publicly available and how is compliance maintained?
2) Does (the Sponsor) have a dedicated stewardship evaluation team? If so, when was the team established and how many professionals are on the team?
3) In the past five years, how many professionals have been added to the stewardship team?
4) What training or resources does (the Sponsor) provide to investment professionals to help staff keep abreast of emerging stewardship and ESG-related issues?

### Disclosure

1) Please include voting records for FY 2021. (If possible, please provide attached voting records rather than the SEC website link).
2) Does (the Sponsor) utilize corporate reporting frameworks for firm level disclosure? If so, what frameworks does (the Sponsor) utilize (e.g., SASB, TCFD, GRI etc.)?
  a. If not, is (the Sponsor) considering reporting under specified frameworks or standards to create consistent comparable disclosure and what is the timeline?

### Climate Initiatives

1) What are the guiding principles for (the Sponsor)'s climate strategy?
2) Please provide an overview of how climate change is considered within (the Sponsor)'s process and outline how carbon risk is measured.
3) Does (the Sponsor) consider TCFD standards and recommendations within the investment process?
4) Describe (the Sponsor)'s climate-related engagement strategies and scope. Please provide examples of climate-related engagements.
5) Does (the Sponsor) monitor portfolio companies' oversight of climate-related risks and/or climate-related opportunities?
6) In general, does (the Sponsor) vote for resolutions requesting that portfolio companies disclose information on climate change risks and how they are managed? (i.e., financial, physical, or regulatory risks they

# 2022 ETF Stewardship Survey Questions

face related to climate change effects on operations and investments.)
7) Please provide (the Sponsor)'s climate-specific voting record for FY 2021.

### Diversity, Equity, and Inclusion

1) Does (the Sponsor) have a stated diversity and inclusion policy? Please attach.
2) Does (the Sponsor) monitor and report on demographic information of its employees?
3) Does (the Sponsor) have an intentional diversity and inclusion plan to promote equity at all levels of the company, including management, executive, and board levels?
4) Does (the Sponsor) have policies that are intended to increase the level of gender and ethnic diversity of senior leadership and investment teams?
   a. If yes, does (the Sponsor) track KPIs related to staff diversity initiatives?
   b. If yes, does (the Sponsor) make KPI reporting available to external parties?
5) Does (the Sponsor) have a mentorship program available for women/minorities?
6) Has (the Sponsor) undertaken a gender or ethnic diversity pay gap study?
   a. If yes, are there policies in place to remedy any deficiencies found?
7) Does (the Sponsor) have a pay-parity policy in place?
8) What percentage of (the Sponsor)'s stewardship team/investment team:
   a. Are military veterans?
   b. Are disabled?
   c. Identify as female?
   d. Identify as a racial/ethnic minority?
9) Does (the Sponsor) track the diversity and inclusion statistics of portfolio companies? If so, please explain.

### Sponsor Level Governance

1) What is the average tenure of (the Sponsor)'s board members?
2) What is the gender and racial/ethnic minority representation of (the Sponsor)'s board members?
3) What are the compensation and remuneration policies of (the Sponsor) for C-suite executives?
4) What percentage of (the Sponsor)'s board members are independent? Is the (the Sponsor's) CEO also the Chairman of the Board?
5) What are (the Sponsor)'s lobbying and political donation policies?
6) Does the (the Sponsor) have a whistleblower policy? If yes, please describe.
7) Does (the Sponsor) have an ethics code and/or code of conduct? If yes, how often are updates made?
8) Does the (the Sponsor) have past or ongoing legal proceedings associated with fraud, insider trading, anti-trust, anti-competitive behavior, market manipulation, malpractice, or other related financial industry laws or regulations? If so, what are the total amount of monetary losses as a result?
9) Does (the Sponsor) have a sexual harassment policy? If yes, how often are employees required to review/sign compliance of it?

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