

Dear Sir/Madam

EOS at Federated Hermes engages with companies around the world on behalf of global institutional investors, representing assets of €1.5tn (30 September 2021). We aim to deliver sustainable wealth creation that enriches investors, benefits society and preserves the environment – for current generations and those to come. This aim informs our expectations of the companies in which we and our clients are invested.

It is our strong belief that companies can only create and preserve long-term, good quality returns for investors if they provide goods and services that sustainably solve societal needs, guided by a clear purpose that serves not only shareholders, but also other stakeholders, society and the environment. Doing this effectively requires robust governance and a healthy culture, with leadership that sets the right tone from the top and emphasises ethical values across the organisation.

### **Corporate Governance Principles – The Netherlands**

Our expectations are set out in more detail in our 2022 Corporate Governance Principles of the Netherlands, which are enclosed. We would like to highlight the following expectations for Dutch-listed companies in 2022:

- **Climate change:** Earlier this year, the international business of Federated Hermes signed up to the Net Zero Asset Managers initiative (NZAM). This initiative now has the support of 220 signatory managers with \$57 trillion of assets under management<sup>1</sup> (55% of global AUM). Signatories to NZAM have committed to “implement a stewardship and engagement strategy, with a clear escalation and voting policy, that is consistent with [the] ambition for all assets under management to achieve net zero emissions by 2050 or sooner.” In 2022, we will continue to hold the chair or other responsible directors accountable through our voting recommendations where we believe companies’ actions are materially misaligned with the goals of the Paris Agreement, where company disclosures or responsiveness are insufficient. We assess companies using a range of frameworks and benchmarks, including the Transition Pathway Initiative (TPI)<sup>2</sup>, the Climate Action 100+ benchmark<sup>3</sup>, Forest 500<sup>4</sup> and others. In principle, we support the emergence of so-called ‘Vote on Transition’ or ‘Say on Climate’ resolutions and will support those plans aligned to the goals of the Paris Agreement, as indicated by short, medium and long-term science-based greenhouse gas reduction targets and a clear and credible strategy to achieve these.
- **Diversity, equity and inclusion:** Many companies continue to fall short of reflecting the diversity of society on their boards, in senior management and throughout the workforce. We strongly advocate for supervisory and management boards of diverse composition, in its broadest sense, and for the execution of meaningful workforce-level diversity, equity and inclusion strategies.

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<sup>1</sup> <https://www.netzeroassetmanagers.org/>

<sup>2</sup> <http://www.lse.ac.uk/GranthamInstitute/tpi/the-toolkit/>

<sup>3</sup> <https://www.climateaction100.org/progress/net-zero-company-benchmark/>

<sup>4</sup> <https://forest500.org/>

In 2022, we will expand our policy to recommend voting against resolutions at companies that we judge to be making insufficient progress on diversity, including:

- We expect at least 30% representation of each gender on the supervisory board, in line with legal requirements, and will generally recommend voting against the election of the nomination committee chair or other members of the nominations committee where this is not the case.
- We expect companies to work towards 30% representation of each gender on the management board and make robust plans to develop a pipeline of strong female candidates. We will generally recommend voting against the election of the nomination committee chair or other members of the nominations committee for AEX and AMX companies that have no female directors on the management board.
- **Human and labour rights:** How a company manages its human rights strategy is of critical importance to its licence to operate, its impact on people's lives and ultimately its ability to create and preserve long-term holistic value. Starting in 2022, we will consider recommending votes against relevant proposals, including the election of directors or their discharge, where a company is in clear breach of its applicable regulatory responsibilities or those outlined in the UN Guiding Principles on Business and Human Rights, and/or if there is sufficient evidence that a company has caused or contributed to egregious, adverse human rights impacts or controversies and has failed to provide appropriate remedy.
- **Executive pay:** We continue to make the case for simpler pay schemes aligned to long-term strategy and the desired culture in the organisation, with an emphasis on long-term share ownership for executives. We seek to understand how executive remuneration decisions are made with consideration to a company's broader stakeholders and expect the board to intervene and apply appropriate discretion where pay outcomes do not align with these expectations.

In our 2022 voting guidelines for Netherlands, consistent with previous years, when a remuneration system does not show sufficient progress towards our expectations, we will recommend voting against the policy and under certain circumstances escalate to voting against the discharge of the chair of the supervisory board. Insufficient progress could, for instance, be demonstrated by a lack of shareholding guidelines for the management board, misalignment of pay and performance, and over-reliance on financial as opposed to strategic metrics in the long-term incentive plan. Further detail on our voting guidelines regarding executive pay can be found in the Principles.

We welcome any comments and observations on our 2022 Corporate Governance Principles and would be glad to answer any queries or concerns they may raise.

Yours sincerely



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# Corporate Governance Principles

## The Netherlands

Our expectations of companies  
incorporated in The Netherlands

**EOS at Federated Hermes  
2022**

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## **Corporate Governance Principles: Our expectations of publicly-listed companies**

**2022**

### **INTRODUCTION**

EOS at Federated Hermes is a stewardship service provider representing a broad range of long-term institutional investors. EOS clients seek to be active stewards of their beneficiaries' assets by being active owners of shares or debt of the companies in which they invest. EOS engages with our clients' investee companies around the world to promote long-term, sustainable returns to investors, their beneficiaries, and other stakeholders.

These Principles express our expectations of board directors and companies across a number of important strategic and governance topics, focusing on areas which will inform the policies which guide our voting recommendations for 2022.

This document is not exhaustive. More detail on our expectations, particularly on environmental and social topics, can be found in our Public Engagement Plan,<sup>1</sup> which is updated annually.

### **COMPANY PURPOSE, CULTURE AND ETHICAL LEADERSHIP**

The board must set and find effective ways to oversee the values of the organisation, that must be founded on ethical integrity. Ethical considerations must underpin every decision made by the board. For example, the board must ensure that its CEO has the highest ethical standards and must not accept any lapses in that expectation during the CEO's time in office or beforehand, performing sufficient due diligence and having strong contractual provisions to enable the board to take sufficient action, including clawing back pay and dismissal for cause, should unethical behaviour come to light.

The board must ensure that a system exists to take multiple different soundings of the culture and micro-cultures in different parts of the organisation and guarantee that both the board and management take action to improve the culture where it is not aligned with the board's expectations. This should include robust and accessible whistleblowing systems together with a demonstrable commitment to protect those that use such systems.

It is our strong belief that companies can only create and preserve long-term, good quality returns for investors if they provide goods and services that sustainably solve societal needs. To achieve this, we expect companies to be guided by a purpose that serves not only shareholders, but also other stakeholders, society and the environment. Achieving this purpose will, in turn, require a healthy culture and an emphasis on ethical values across the organisation. The pursuit of a stakeholder-inclusive purpose in support of long-term societal interests will then help protect the long-term interests of the savers and pensioners – current and future – invested in companies, who require sustainable financial returns and an economy, society and environment

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<sup>1</sup> The latest public version of the EOS Engagement Plan can be found at: [www.hermes-investment.com/stewardship/eos-library](http://www.hermes-investment.com/stewardship/eos-library)

which can provide a secure future. This will require review of those critical ESG-related issues of concern to the company and its stakeholders, such as climate change or human rights, through an ethical lens.

A clear and meaningful business purpose should enable business leaders to identify the right things to do in the short term, in order to fulfil their purpose over the long term. This is critical in a time of crisis – such as that caused by the Covid-19 pandemic – when difficult trade-offs arise, particularly between shorter-term financial returns and maintaining strong relationships with key stakeholders, including government, the workforce, customers and supply chains.

As the effects of the pandemic continue to be felt around the world, it remains vital that boards and executive teams continue to consider their key stakeholders and their organisation's purpose, and make decisions that best support sustainable returns over the long-term. Companies need to be able to explain their decisions affecting key stakeholders. This includes the most difficult decisions, such as redundancies, but also how they allocate capital, including dividend payments and share buybacks.

We expect boards to consider and disclose capital allocation policy in the context of a company's purpose and long-term strategy. We are concerned that buybacks and similar diversions from re-investment in key stakeholders may be chosen to improve the share price or other related metrics over the short-term but are not always the best use of capital to support the creation of long-term, sustainable returns.

We are supportive of alternative corporate structures that explicitly mandate the consideration of key stakeholders alongside shareholders, where companies believe this to be beneficial in service of their purpose.

### **Stewardship and engagement**

Investors must act as responsible stewards and promote long-term sustainable returns on investment through constructive engagement with companies and their directors. All substantive correspondence from major institutional investors' representatives should be shared promptly with all board members to help directors fulfil their role to safeguard the interests of all shareholders. Our experience has shown that dialogue between companies and committed, long-term investors on strategy, finance, risk management and material environmental, social and governance (ESG) issues can improve the governance and performance of companies. Developing relationships of trust with long-term shareholders can be invaluable for boards, and we expect chairs and independent directors to make themselves available for investor engagement, beyond opportunities at formal shareholder meetings.

We expect companies to engage with long-term investors across a range of asset classes, including different types of corporate debt, in addition to their shareholders. Companies should now recognise that the expectations of debt investors are similar to those of long-term shareholders and substantially aligned in relation to governance, long-term strategy, capital allocation and environmental and social matters. Debt investors now expect accountability and

constructive dialogue on opportunities and risks which might enhance or impair earnings and cashflow.

## ENDORSEMENT OF THE DUTCH CORPORATE GOVERNANCE CODE

We generally support the recommendations of the Dutch Corporate Governance Code (the Code)<sup>2</sup> and encourage companies to comply with these or to explain their reasons for any non-compliance. We also support the additional guidance provided by the Eumedion Corporate Governance Manual.<sup>3</sup>

## BOARD COMPOSITION AND EFFECTIVENESS

Supervisory boards should ensure they comprise members with strong ethics and diverse skills, experience, perspectives and psychological attributes, as well as sufficient independence and strength of character to challenge, as well as advise and support executive management teams. They should ensure overall composition and individual membership of the supervisory board is frequently reviewed and refreshed, and that directors are elected and re-elected by shareholders on a regular basis to ensure accountability. Biographies for all directors should be provided to shareholders, indicating which are considered independent and the particular attributes that they bring to the board. This should be accompanied by an analysis of how the supervisory board as a whole displays the necessary skills, independence, diversity and other attributes to meet the company's evolving needs.

### Effectiveness

Disclosure of measurable aspects of supervisory boards, such as those outlined below, are important but insufficient indicators of a board's functionality.

Engagement with board directors provides a valuable opportunity for investors to sufficiently assess how well a board is functioning. Our white paper, *Guiding Principles for an Effective Board*,<sup>4</sup> highlights the factors that we consider to be most important in determining board effectiveness, focusing on the human, relational, and behavioural elements that are more difficult to assess.

They can be summarised as follows:

- Genuine independence, diversity and inclusion support directors' ability to effectively question long-held assumptions and mitigate the risk of groupthink.
- The role of the chair should be held by an independent director<sup>5</sup> to support the overall conditions for board effectiveness, which includes setting and enforcing the expectations for a board culture that is based on mutual respect, openness and trust, and encouraging diverse voices and behaviours of independent thinkers.

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<sup>2</sup> In December 2016, the Corporate Governance Code Monitoring Committee published the revised Dutch Corporate Governance Code 2016 [English. Publicly traded Dutch companies are to follow this Code on a comply-or-explain basis in their annual accounts. The revised Code has given a central role to long-term value creation, and the introduction of 'culture' as a component of effective governance.](https://www.mccg.nl/english) <https://www.mccg.nl/english>

<sup>3</sup> Eumedion is a Dutch foundation representing the interests of institutional investors with investments in Dutch listed companies. <https://en.eumedion.nl/Themes/corporate-governance.html>

<sup>4</sup> <https://www.hermes-investment.com/wp-content/uploads/2020/04/guiding-principles-for-an-effective-board-april-2020.pdf>

<sup>5</sup> See paragraph Governance structure below. The Netherlands traditionally works with a dualistic governance model (two-tier governance structure). The large majority of Dutch companies choose this model, however the option of a unitary board governance model is used by a number of companies.

- How the board allocates its time spent in board meetings and between board meetings is equally important. We expect a board to maximise the time spent on strategy and other forward-looking activities during structured board meetings, committee work, site visits and engagement with stakeholders.
- The board's relationship with the CEO should ideally be characterised by transparency, trust and constructive collaboration, and the board should build relationships with the wider workforce through formal and informal channels.
- A commitment to continuous improvement should be encouraged and supported through regular board evaluations, and disclosure should strike a balance between transparency and confidentiality.

### Evaluation

We expect supervisory boards to be committed to continuous improvement and therefore to be constantly reflecting on their performance. We encourage boards across markets and corporate structures to conduct regular evaluations with the goal of enhancing board effectiveness. When conducted with this intention, and not simply as a compliance exercise, the evaluation process offers a unique opportunity for the board to pause, reflect and optimise its performance. The board should embrace the evaluation process as an opportunity to recalibrate focus, identify skills gaps on the board, highlight the need for succession, and raise concerns related to performance and culture.

Furthermore, conducting regular board evaluations signals to investors that the board is open to constructive criticism and willing to improve. We recommend that independent external board evaluations are conducted at least once every three years, with internal evaluations conducted in the interim years. The board should implement an action plan and a clear timeline for addressing the points raised in the evaluation. Disclosure should demonstrate how the board has taken the necessary steps to enhance performance and provide reassurance to investors about the quality of the board evaluation.

### Governance structure

The Netherlands traditionally works with a dualistic governance model<sup>6</sup> (i.e. a two-tier governance structure). The large majority of Dutch companies choose this model, however the option<sup>7</sup> of a unitary board governance model is used by a number of companies.

When a two-tier structure is applied, the company's articles will provide for a management board consisting of executive directors, and a supervisory board consisting of non-executive directors (also called supervisory directors). There are several variations in structures and related requirements for two-tier boards.

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<sup>6</sup> Ever since the world's first publicly traded company, VOC (the Dutch East India Trading Company) established a two-tier board in 1623 in response to governance concerns.

<sup>7</sup> This option was introduced in Dutch company law with the amendment of the Dutch Civil Code that entered into force on January 1st 2013.

In the majority of Dutch listed companies, the supervisory board nominates and shareholders elect both the supervisory board and the management board.

Under Dutch law, companies that meet certain thresholds<sup>8</sup> of share capital and number and location of employees are considered to be 'large' companies and are legally required to implement the structure regime (structuurregime), which further limits the powers of the management board in favour of the supervisory board.

Around a quarter of the Dutch listed companies follow the structure regime. If the structure regime is in place, the annual shareholders' meeting does not have the power to appoint or dismiss management board members. This power resides with the supervisory board. The supervisory board also has the right of approval for several important decisions of the management board. The annual shareholders' meeting appoints and dismisses the supervisory board, but the works council – representing company employees – has a strong influence on this appointment process, with nominating rights for up to one third of the seats on the supervisory board.<sup>9</sup>

Companies with a one-tier governance structure have a single management board comprising executive and non-executive directors. In this situation, the latter oversee the former, and there is no supervisory board. It is important that independent oversight by non-executive directors is sufficiently ensured. The majority of a unitary board should be made up of independent, non-executive directors and committees should comprise exclusively non-executive directors. The chair of the one-tier board may not also be an executive director.

### Independence and tenure

On all supervisory boards, we expect a strong core of independent directors to ensure that stakeholder interests are protected, to exercise objective judgement and, if necessary, to act as agents for change. This group should play an important role in guiding the boards' decision-making and in the recruitment and nomination of directors. It should be empowered to meet independently, including before and after board meetings, and should do so in practice. It should be granted unfettered access to members of management, information and resources as required.

Ensuring sufficient levels and quality of independence is particularly important for companies that are founder-led or have representatives of significant shareholder representatives on the supervisory board (which we believe can be useful and justified, provided minority shareholder interests are protected). We contributed to and support a position paper by Eumedion<sup>10</sup> with proposals to better safeguard the interests of minority shareholders at companies with a controlling shareholder.

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<sup>8</sup> According to Book 2, Article 153(2) of the Dutch Civil Code, in order to qualify as a 'large company', a company must have an share capital of at least €1.6 million, employ at least 100 employees in the Netherlands.

<sup>9</sup> Employees of a company or trade union officers directly involved in collective bargaining are excluded from nomination onto the supervisory board. As a consequence, works councils often rely on the nomination to the board of candidates that have demonstrated a certain commitment to the workers' interests (former trade unionists, politicians, industrial relations and human resources experts).

<sup>10</sup> <https://en.eumedion.nl/clientdata/217/media/clientimages/2016-06-position-paper-minority-shareholders-final-version.pdf?v=200919161644>

In accordance with Dutch Corporate Governance Code,<sup>11</sup> we generally recommend that the majority of supervisory board members should be independent. In addition, we expect that the majority of the members who serve on the supervisory board's remuneration and selection and appointment committees to be independent. For improved audit committee effectiveness, we expect all members of the audit committee to be independent. In their disclosures, companies should clearly state which directors they consider to be independent and the criteria by which independence is determined.

We expect a healthy mixture of tenures on boards, supported by regular board refreshment. We consider the overall composition of boards and recognise the value that long-serving directors can contribute. However, too many directors serving concurrently can increase the risk of groupthink and complacency.

### Committees

We expect larger supervisory boards<sup>12</sup> to have specific board committees covering audit, risk, executive remuneration and board nominations. For some companies, additional committees may be required to cover other material issues, for example a sustainability committee for environmentally-exposed companies. For those smaller boards that choose to address these matters at full board meetings, there should be clear narrative reporting to demonstrate these receive adequate time and attention.

### Director attendance and commitment

We expect board directors to be able to devote sufficient time to fulfil their duties, including to build and maintain a good understanding of the company and to fully absorb and be able to challenge the information presented to them by management. As a broad guideline, we do not support directors holding more than five directorships at public companies and, in this context, we consider a non-executive chair role to be roughly equivalent to two directorships and, at complex companies, other committee chair roles, in particular the chair of the audit and risk committee, may be considered more burdensome than a typical non-executive directorship.

Whether a director may be over-committed depends on a range of factors beyond the number of other roles they hold, including the size and complexity of the company and additional responsibilities, such as being a committee chair. We consider that certain industries such as banking (due to its business model and regulatory complexity) and businesses with large and/ or complex operations will require site visits and therefore more time commitment.

We expect companies to encourage their executives to take on a non-executive role (but not normally more than one) outside their own company to assist in their development, bring current experience to boards and to build a pipeline of future board directors.

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<sup>11</sup> The Dutch Corporate Governance Code - best practice provision 2.1.7 - Independence of the supervisory board

<sup>12</sup> The Dutch Corporate Governance Code – best practice provision 2.3.2 – Establishment of committees: If the supervisory board consists of more than four members, it should appoint from among its members an audit committee, a remuneration committee and a selection and appointment committee.

## Succession planning

Effective succession planning at the supervisory board and senior management level is essential for safeguarding the ability of companies to deliver long-term returns. It should involve contingency planning for the sudden loss of key personnel, as well as planning for foreseeable change such as impending retirement. It should include consideration of the current and future required diversity of skills, experience and other attributes required at board and senior management level, including the need for any candidate to demonstrate the highest levels of ethical integrity. Robust succession planning also can help to counter the tendency of many supervisory boards to over-pay current executives relative to the senior executive labour market and peers.

Overseen by the supervisory board, senior management should create a pipeline of suitable candidates from within the organisation to become senior managers and executive directors.

## Granting discharge

The discharge of the management board and of the supervisory board are standard voting items in the Netherlands on the agenda of the annual shareholders' meeting. In legal terms, discharge means that the policy of the executive board and the supervision of the supervisory board, as conducted until the moment of discharge, are approved by the meeting.

Discharge is only a waiver of liability for executive and supervisory directors. Third parties are still able to invoke liability of directors. Under normal circumstances the discharge voting items generally receive high levels of support. Not receiving discharge does not have any direct consequences, while receiving discharge does not affect the shareholders' rights to bring legal action against directors for breaches of their duties when unknown facts surface after the discharge is granted.

We see voting against discharge as a corrective gesture; somewhat similar to giving a 'yellow card' in a football match. We will recommend a vote against the discharge to express our dissatisfaction with one or more decisions made and/or with a disappointing performance of the executive and/or supervisory board, without submitting a motion of no confidence in the executive and/or the supervisory board. In making our decision in relation to the discharge of the board we will consider:

- Is legal action still pending against the company, a member of the management board or a member of the supervisory board?
- If the financial statements are not adopted, granting discharge to members of the management board and members of the supervisory board is not an obvious course of action.
- Has the management board responded adequately in the previous financial year to the remarks of the shareholders with regard to the strategy and policy of the management board? Has the supervisory board played a good, mediating role in this context?
- Has the management board of the company responded adequately to the recommendations made by shareholders in previous general meetings?

- Is the degree of compliance with the Dutch corporate governance code sufficiently high, or have reasons that are acceptable from the perspective of institutional investors been provided for the non-compliances with the provisions of the code?

## DIVERSITY, EQUITY AND INCLUSION

Beyond the clear moral and ethical imperative, the system-wide benefits of social and economic inclusion and the risks of continued exclusion, a growing body of evidence supports the link between more diverse company leadership and financial performance.<sup>13</sup> We believe improving diversity, equity and inclusion performance creates enduring value by improving decision-making, attracting talent, enhancing workforce satisfaction and stimulating insight and innovation.<sup>14</sup>

Recent tragic events, including George Floyd's murder in the US in May 2020, have brought into focus glaring racial and ethnic injustices around the world that are reflected on boards and in workforces, including those of companies' suppliers and in unfair impacts of business practices on diverse communities. In many parts of the world, Mr Floyd's death triggered difficult conversations that exposed barriers, in the workplace and elsewhere, faced by diverse groups, including but not limited to race, ethnicity, gender, sexual orientation, age, disability, nationality and socioeconomic background; and highlighted the additional challenges that individuals who belong to multiple diverse groups experience. It also focused attention on the need to build more inclusive company cultures that dismantle obstacles and enable all individuals to thrive and maximise their contributions to their companies, communities and society.

Discrimination against persons from different ethnic and migration backgrounds is an issue that must be addressed in the Netherlands as well. In 2020, the population of the Netherlands stood at 17.4 million, including over 4 million (24%) people with a migration background.<sup>15</sup> Although the gap between the socio-economic position of people with a migration background and people with a non-migration background has narrowed in the past decade, people with a migration background are still in a less favourable position than people with a native Dutch background. On average, they have a lower level of education and a lower level of income, are less likely to be in employment and are more likely to be benefit-dependent. People with a migration background are also less likely to experience their health as good or very good. On average, people with a non-western migration background<sup>16</sup> are more disadvantaged than people with a western migration background.

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<sup>13</sup> For example, The 30% Club has compiled a list of studies examining the benefits of gender diversity <https://30percentclub.org/initiatives/investor-group>

<sup>14</sup> For example, [Delivering growth through diversity in the workplace | McKinsey](#)

<sup>15</sup> [Population Outlook 2050: more people with a migration background \(cbs.nl\)](#)

<sup>16</sup> The Dutch Central Agency for Statistics (CBS) defines a person with a non-western background as a person originating from a country in Africa, South America or Asia (excl. Indonesia and Japan) or from Turkey. Due to their socioeconomic and cultural position, people from Indonesia and Japan residing in the Netherlands are considered as having a 'western' migration background. These are mainly people born in the former Dutch East Indies and expatriates employed by Japanese companies with their families.

The Social and Cultural Planning Office (SCP) of the Dutch government published a report in 2020 describing the nature and extent of discrimination in the Netherlands.<sup>17</sup> According to the report, one quarter of inhabitants of the Netherlands experienced one or more incidents in 2018 which they perceived as discrimination. The report also presents a picture of different groups' experiences with discrimination. The report finds that Dutch citizens with a Moroccan and Turkish background, and Muslims, encounter a great deal of both negative attitudes and unequal treatment. They are heavily stigmatised in Dutch society and are perceived as threatening by a proportion of the majority group.

In 2022 we will continue tightening our voting policies and thresholds on diversity, as we believe most companies need to improve their diversity towards representation of all groups throughout all roles and levels. Boards should seek diverse composition in its broadest sense to support high-quality debate and decision-making, considering diversity of skills, experience, networks, psychological attributes and characteristics (including, but not limited to, race, ethnicity, gender, sexual orientation, age, disability, nationality and socioeconomic background). Boards should give careful consideration to how they can find members from outside of their typical networks and the breadth of attributes or perspectives that may be valuable to their decision-making. Where boards have made insufficient progress on critical dimensions of diversity, including racial and ethnic or gender representation at either board and senior management level, we will recommend opposing the re-appointment of relevant responsible directors.

We welcome recent regulatory mandates and voluntary commitments in some countries. The integration of targets for representation of people of colour and women by the 30% Club encourages boards to strategically prioritise racially- and ethnically-diverse director recruitment and set thresholds for gender representation. In August 2021, the US Securities and Exchange Commission (SEC) approved Nasdaq's Board Diversity Rule, which requires disclosure of board diversity statistics and at least two diverse directors including one female and one under-represented racial minority or LGBTQ+ director.<sup>18</sup> However, we note that some racial and ethnic groups are much less likely to obtain board roles than others, reflecting societal bias and we expect boards to address these biases.

At the request of the Dutch Government, the Social and Economic Council of the Netherlands (SER) issued an advisory report 'Diversity in the boardroom: Time to accelerate'<sup>19</sup> in 2019, which discusses the obstacles to greater cultural and gender diversity in the boardroom and possible solutions. The Netherlands has fewer women in management positions than many other European countries. Many people with a non-western migration background have trouble moving up the ranks to a more senior position.

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<sup>17</sup> <https://www.scp.nl/publicaties/publicaties/2020/04/02/ervaren-discriminatie-in-nederland-ii>

<sup>18</sup> See Rule [Board Diversity Disclosure Five Things.pdf \(nasdaq.com\)](#)

<sup>19</sup> <https://www.ser.nl/-/media/ser/downloads/engels/2019/diversity-boardroom.pdf>

In September 2021 the Dutch senate approved a bill for a more balanced ratio between men and women in the board of directors and supervisory board. The bill is based on advice from the Social and Economic Council and likely to come into force on January 1<sup>st</sup> 2022. The new bill requires companies listed in the Netherlands to have at least one third of their supervisory board seats held by women. Companies that fail to meet the minimum threshold will have to replace any board position left by a man with a woman, or face leaving that position empty. In addition, listed companies with more than 250 employees must set “appropriate and ambitious targets” for the number of female executives and senior managers.

We expect supervisory boards not only to address their own diversity, but that of the whole organisation and its impacts on stakeholders; and to provide meaningful disclosure assessing progress against complex challenges. In 2022, we will hold supervisory boards accountable for more effective oversight of inclusive culture and diversity across all levels of the company's workforce and effects on the ecosystem upon which the company's long-term health depends, including suppliers, customers and communities. When developing director voting recommendations, we will take into account a range of considerations. From a workforce perspective, these may include, but are not limited to, diversity of named executive officers, senior executive team members and talent pipeline; the existence of a thoughtful diversity, equity and inclusion strategy, targets and action plan rooted in rigorous analysis of underlying problems that incorporates employee survey data; and a board-driven process for evaluating management's inclusion performance and issues surrounding all strands of diversity across the employee lifecycle.

### EXECUTIVE REMUNERATION

We are increasingly concerned that executive remuneration structures and practices in a number of countries are not fit for purpose, neither serving long-term investors nor aligning properly with the core long-term objectives of companies, and that poor practices are at risk of spreading to other countries where pay is more restrained.

Some of our key concerns relate to the limitations of ‘pay for performance’ models, which are common in countries like the US and the UK and which we see increasingly adopted in other countries. Although perhaps well-intentioned, this approach risks damaging, unintended consequences, including:

- Increasing quantum beyond the executive labour market median, and expanding pay disparities between executives and the broader workforce
- Encouraging short-termism or financial engineering, particularly in schemes which focus on share options or where large proportions of pay are subject to metrics like total shareholder return or earnings per share, which can focus executives on actions to drive up the share price in the short-term rather than on drivers of long-term strategic value. Focusing large portions of pay on incentive schemes risks strongly incentivising executives to hit targets over relatively short time frames, regardless of whether these actions are best aligned to long-term, high-quality sustainable returns to shareholders and other stakeholders.

- Obscuring meaningful assessments of performance in the context of long-term value due to the use of complex, overlapping incentive schemes.
- Undeserved windfall gains for executives which can result from share-based incentive schemes, which has occurred at many companies as a result of the market rally that followed government interventions in the wake of the Covid pandemic.

We continue to make the case for switching to simpler pay schemes aligned to long-term success and the desired culture in the organisation, based on a combination of fixed pay and long-term time-restricted stock, with an emphasis on long-term share ownership for executives.

We expand on our views on executive pay in our paper, *Remuneration Principles: Clarifying Expectations*.<sup>20</sup>

They can be summarised as follows:

1. **Simplicity:** Pay should be simple; for example, fixed pay (mix of cash and long-term shares) plus a single incentive scheme (an annual bonus).
2. **Alignment:** Pay should be aligned to long-term strategy and the desired corporate culture, incentivising long-term value creation, including wider social and environmental outcomes. Where metrics and targets are used in incentive pay, they should reflect strategic goals, rather than focus attention on total shareholder return, stock price appreciation or earnings per share.
3. **Shareholding:** Management should become long-term stakeholders in the company's success through substantial shareholdings. Significant shareholding requirements should remain in place for at least two years following departure from the company.
4. **Accountability:** Pay outcomes should reflect outcomes for long-term investors and take account of falls in a company's performance or reputation. The board should intervene and apply discretion whenever formulaic outcomes do not achieve this. The potential pay outcomes under a policy should be rigorously scenario tested in advance, with a cap on the total possible pay published, to help reduce the risk of unintended consequences.
5. **Stewardship:** Pay outcomes should be communicable to all stakeholders, including employees and the public. Boards should take into account wider workforce pay practices and ratios when judging the appropriateness of pay opportunities and outcomes. Boards should then write to employees each year explaining the outcomes of executive pay and the alignment to long-term value, and the company's strategy and purpose. Companies and investors should regularly discuss strategy, long-term performance and the link to executive pay.

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<sup>20</sup> <https://www.hermes-investment.com/wp-content/uploads/2018/10/remuneration-principles-clarifying-expectations.pdf>. The principles contained in this paper are global in nature, but some of the specific references to structures are more applicable to certain markets such as the UK.

While we do not automatically oppose all pay models that do not appear to align to our principles, we set various thresholds and requirements to guide our voting recommendations which are tailored to the context of each market. Through engagement with companies on these thresholds and requirements, we seek to improve market practice and encourage closer alignment with our principles.

At present, in the Netherlands we take the approach of setting a number of pragmatic guidelines and thresholds in our voting policy to improve market practice and encourage closer alignment with our principles. In 2022 we will consistently apply key expectations communicated in 2021 including:

- **Executive shareholdings:** Management board members and senior executives should be required to invest in or be paid in shares and hold a significant amount of equity over the long term. Ownership of shares over the long term is the best form of alignment between executives and shareholders. In the Netherlands, we expect to see minimum shareholding requirements equivalent to 300% of salary for AEX companies and 200% for all other companies. We may vote against a remuneration policy that has no specified shareholding requirement.
- **Fixed to variable pay opportunity** Our guideline is that a ratio of more than four times base salary is concerning, and more than six times is unlikely to gain our support without a compelling justification.□
- **Alignment of performance metrics to strategy:** Variable remuneration should be based on metrics that align to long-term strategic value and the company's sustainable performance in comparison with its peers. These should reflect long-term company objectives, derived from the company's strategy, and should include material sustainability parameters (e.g. innovation, environmental and social impact, corporate culture, customer service and employee satisfaction) alongside strategic and financial objectives. We will generally oppose schemes which use TSR, whether relative or absolute, as their dominant metric.

### Say on pay

Following the implementation of the revised EU Shareholder Rights Directive (SRD II),<sup>21</sup> all Dutch listed companies were required to submit their 2019 remuneration report for an advisory vote to the 2020 AGM and a large majority also had to renew their remuneration policy for the executive and supervisory directors. Such a new remuneration policy needs the support of at least 75% of the votes cast in a general meeting, if the company's articles of association do not stipulate a lower majority. In addition, companies are since then also required to explain how the remuneration policy takes the 'social acceptance' into account.

In the event of egregious pay practices or when we issue a negative vote recommendation on remuneration-related proposals for the second time in a row, we will hold the remuneration committee chair accountable and recommend a vote against his/her re-election.

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<sup>21</sup> <https://wetgeving.skalender.overheid.nl/Regeling/WGK008744>

## PROTECTION OF SHAREHOLDER RIGHTS

We rigorously defend shareholder rights on behalf of institutional investors, including the right to receive good quality corporate reporting and material information on a timely basis, to vote at shareholder meetings on issues such as the annual election of directors, to propose new candidates to the board or other shareholder resolutions.

We support a single share class structure, with one share one vote, and oppose any deviation from this.

### Hybrid or virtual shareholder meetings

Annual and other shareholder meetings are a critical part of corporate governance. As well as being the highest decision-making procedure of the company, they allow shareholders to hear directly from the company about its performance and to challenge directors on important topics, supporting strong transparency and accountability.

We believe dialogue between shareholders and the board is enhanced by the in-person meeting format of annual meetings. Although formats vary around the world, when working well, it presents the opportunity for shareholders to make points to the whole board, the ability to ask questions immediately in response to board comments and to build on the questions asked by others. Further, it is more difficult for directors to avoid challenging questions or topics; directors must provide answers in a public forum and, accordingly, be accountable for them.

However, we recognise that the restrictions brought about by the Covid-19 pandemic rendered in-person meetings unviable for many companies and that there were already valid arguments in favour of adopting alternative formats to improve shareholder access and participation, for example, in geographically dispersed countries or for companies with a global shareholder register.

Given this, we are supportive of meetings being convened in a 'hybrid' format – where shareholders have the option to join the meeting via an online platform or to join in person, provided all shareholder rights are protected or enhanced in both formats. Online participation can increase opportunities for participation, while retaining the accountability of in-person meetings.

We do not generally support 'virtual-only' meetings unless these are a temporary solution in response to restrictions on in-person gatherings, such as those prompted by the Covid-19 pandemic, or other exceptional circumstances. In those cases, we expect all shareholder rights to be protected and the meeting to be run as it should be in-person: giving ample opportunity for any shareholder to ask questions, and for these questions to be answered live by the board. We also expect a clear commitment to return to in-person or hybrid meetings as soon as restrictions allow.

For further information please refer to our *[Principles of Annual Meeting Good Practice](#)*.<sup>22</sup>

We will generally oppose requests for the authority to hold virtual-only meetings unless we gain comfort that it is to be used in exceptional circumstances only, and that the rights and access of attending shareholders are comparable to those of in-person meetings. For smaller companies we may relax the expectation that virtual-only meetings are for exceptional circumstances.

### **Meeting notification and proxy documents**

For minority shareholders, the annual general meeting is a formal opportunity to obtain information about management's and the supervisory board's stewardship of their investments and, if necessary, to request clarification of any decisions taken during the year. The annual general meeting is therefore an important accountability mechanism, and the communication of detailed information on all agenda items is a prerequisite for its effectiveness. All documents should be clearly displayed and accessible on the company's website at least 42 days before a shareholder meeting.

### **Multiple class share structures**

Under Dutch corporate law, companies can issue additional voting rights to founders or large shareholders by introducing different classes of shares or granting loyalty voting rights. Multiple-class share structures disenfranchise minority shareholders and often increase the power of one shareholder for a disproportionate economic stake. We encourage issuers with multiple-class share structures to adopt the concept of one-share one-vote for all shares. We are very unlikely to support the issuance of shares with reduced voting rights and capital raising exercises or share buyback schemes that discriminate against minority shareholders.

### **Capital issuance requests**

We are concerned about capital issuance requests from companies, especially requests to issue new capital without pre-emption rights for existing shareholders. We believe that pre-emption rights are an important safeguard for shareholders and their interests in the companies they invest in. Therefore, we generally do not support any proposal for capital issuance without pre-emption rights that would involve the issuance of additional capital of more than 10% of the already outstanding share capital.

### **Share repurchases**

We generally do not support share repurchase programmes which allow companies to buy back shares for a price which exceeds the market price of the shares by more than 10%. We oppose the authorisation of share repurchase programmes which allow companies to buy back more than 10% of the outstanding shares.

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<sup>22</sup> <https://www.hermes-investment.com/ukw/wp-content/uploads/2021/03/eos-principles-of-annual-meeting-good-practice-february-2021.pdf>

## Anti-takeover provisions

Traditionally, the most common anti-takeover measure used by listed Dutch companies is the so-called continuity foundation structure (stichting). The foundation is generally granted a call option for preference shares entitling it to up to 50% of the voting rights at the general shareholders' meeting after the call option is exercised.

While these foundations can often share a long-term perspective with outside minority shareholders, we are concerned that they sometimes have rights that can affect the interests of ordinary shareholders. In particular, we are concerned that foundations can use preference shares to exert influence and control over companies disproportionate to their economic interest.

Companies should disclose the timeframe for any preference share arrangements and we welcome moves by companies or foundations to abolish such structures or introduce sunset provisions, with reasonable and limited timeframes, into them.

Other common anti-takeover measures in the Netherlands are the priority shares structure, the depositary receipt structure and the above-mentioned structure regime. Although the structure regime was originally designed to give employees a stronger position in the company's governance structure, in practice it may have the effect of an anti-takeover measure, as it can make the company less attractive to potential bidders. If the structure regime is applicable, the shareholders' meeting does not have the power to appoint or dismiss management board members. This power resides with the supervisory board.

In September 2020, the bill on the introduction of a statutory cooling-off period for Dutch listed companies was adopted by the lower house of Dutch parliament and introduced to the Senate, which adopted the bill in March 2021.<sup>23</sup> The bill, effective from May 1<sup>st</sup> 2021, allows a management board of a Dutch listed company to invoke a statutory cooling-off period of up to 250 days if one or more shareholders request the company to put a change in the board composition on the agenda of a general meeting, or in the event of a hostile public offer. We believe that directors already have sufficient powers to take account of stakeholder views in the earlier mentioned events and that shareholders should decide the merits of any such approach. Shareholders themselves should take account of their stewardship responsibilities and assess what is best for the long-term success of the company in these situations. We welcome statements by companies that they will not use these provisions.

## Re-domiciling companies

There is a growing, recent phenomenon of companies redomiciling in the Netherlands. Some of the motivation appears to include the antitakeover provisions available in the Dutch market (which we discuss elsewhere in these Principles). However, we are concerned that some of these companies are redomiciling for additional reasons that also put them at odds with the interests of long-term investors and their underlying beneficiaries. These include tax arbitrage to benefit from lower rates of corporate taxation (see the paragraph on tax later in the Principles). We expect all Dutch companies, whatever their history, to live up to the expectations outlined in these Principles and to address

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<sup>23</sup> [Inroepen bedenktijd door bestuur van beursvennootschap \(35.367\) - Eerste Kamer der Staten-Generaal](#)

the most important concerns of their stakeholders and to uphold the highest governance standards and expectations of the Dutch capital markets.

## **SOCIAL, ETHICAL AND ENVIRONMENTAL RESPONSIBILITY**

Taking a responsible and long-term approach to social, environmental and ethical issues is critical to the creation and preservation of long-term sustainable returns and should be reflected in the company's values, purpose, strategy and culture. Companies must identify and disclose the most material social and environmental issues for the company and its significant stakeholders. They must seek to address the associated risks and opportunities through their core business strategy and value proposition. We expect boards and management to have oversight of material sustainability issues and to be accountable to shareholders for effectively managing the associated risks and opportunities.

We support the UN Sustainable Development Goals (SDGs) and believe that the private sector has an important role to play in achieving them by the increasingly pressing deadline of 2030. Companies should assess the relevance of each SDG, identifying those that they can make a direct contribution to, and incorporate the most material SDGs into their strategies. We encourage companies to go beyond highlighting any SDG that the company could be connected to and to be purposeful in selecting those to which it intends to make an active, direct contribution, including through the allocation of resources and setting targets. We urge companies to report on their approach to the SDGs and to engage with its shareholders and civil society on how best to contribute to the SDGs.

Further detail on our views on and expectations of companies with regards to a wide spectrum of environmental and social issues can be found in the EOS Engagement Plan.<sup>24</sup>

Below we highlight two key environmental and social topics which will inform our vote policies in 2022: climate change, and human and labour rights.

### **Climate change**

The breakdown of the climate is a systemic risk to the value of our clients' portfolios, due to the social, economic, and political consequences of climate change.

We strongly support the goal of the 2015 Paris Agreement – to limit global warming to well below 2°C and pursue efforts to not exceed 1.5°C of warming – and we expect companies to publicly do the same, as well as ensuring that any third-party organisations they support or are members of, such as trade bodies or lobbying organisations, are aligned to this goal.

We urge companies to:

- Establish strong governance of the risks and opportunities presented by climate change and the energy transition. Boards should ensure that climate-related issues are included on the board agenda at least annually. We expect the board and senior management to engage with outside

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<sup>24</sup> The latest public version of the EOS Engagement Plan can be found at: [www.hermes-investment.com/stewardship/eos-library](http://www.hermes-investment.com/stewardship/eos-library)

experts who can advise on strategic risks and opportunities that climate change presents, including challenging the company's approach if necessary. For those companies materially exposed to climate-related risks and opportunities, we expect the energy transition to be clearly articulated in governance documents, including board committee charters and the articles of association.

- Commit to achieving net-zero emissions by 2050 at the latest and set supporting short- and medium-term science-based targets to reduce greenhouse gas emissions in line with the goals of the Paris Agreement. This should include material Scope 3 emissions associated with a company's value chain or use of products with an explanation of why any Scope 3 emissions are not included.
- Integrate climate considerations into the forward-looking strategy for the company. Companies should consider the implications of the energy transition on their business, and what aligning to the goals of the Paris Agreement will mean for their strategy, minimising the potential risks and capitalising on the opportunities presented by climate change.
- Adopt the framework set out by the Task Force on Climate-related Financial Disclosures (TCFD) for the management and reporting of climate-related risks and opportunities. Where the risks are particularly acute (for example in energy intensive sectors), this should include conducting scenario analysis to establish the potential financial and other impacts of climate change on the business at different levels of warming. Companies should ensure that the financial risks associated with climate change and the energy transition are appropriately reflected in reports and accounts. As outlined in the Audit section below, the audit committee should be responsible for ensuring these risks are accounted for and the external auditor should be engaged to provide an opinion on this matter.
- Ensure board oversight and robust governance processes are in place to identify incidents of misalignment of views between companies and organisations of which they are members. Where issues are identified, all available avenues to influence these third parties should be used to encourage effective action on climate policy in line with the goals of the Paris Agreement. The company should be transparent about its governance procedures by describing the actions taken to reduce or eliminate any misalignment, and any progress made, in-line with the IIGCC Investor Expectations on Corporate Lobbying on Climate Policy.<sup>25</sup> Ultimately the board should be prepared to cease membership where misalignment persists without progress. Companies should also proactively support and advocate for positive action to mitigate climate change risks in their spheres of influence.

We engage intensively with companies across different countries and sectors on climate change and reinforce this through the voting recommendations we make to our clients at shareholder meetings.

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<sup>25</sup> <https://www.iigcc.org/resource/investor-expectations-on-corporate-lobbying/>

In 2022, we continue to hold the chair or other responsible directors accountable through voting recommendations where we believe companies' actions are materially misaligned with the goals of the Paris Agreement and/or where companies are not responding sufficiently to the risks and opportunities posed by climate change. We include a particular focus on companies that are involved in activities that are clearly incompatible with limiting global warming to safe levels, such as causing deforestation and the expansion of coal-fired power. We assess companies using a range of frameworks and benchmarks, including the Transition Pathway Initiative (TPI),<sup>26</sup> the Climate Action 100+ benchmark,<sup>27</sup> Forest 500<sup>28</sup> and others.

In addition to the above criteria, we may also reflect other concerns about a company's response to climate change in our vote recommendations, for example, where a company has been unresponsive to investor concerns or where we have concerns about the views held by particular directors regarding the reality and urgency of climate change.

We will consider and support on a case-by-case basis shareholder resolutions relating to climate change and may file or co-file resolutions where we believe them to be warranted.

In principle, we support the concept of having a shareholder vote on climate change transition plans (so-called 'Vote on Transition' or 'Say on Climate' resolutions). We will support climate change transition plans which are aligned to the goals of the Paris Agreement, with indicators of alignment including science-based greenhouse gas reduction targets over the short, medium and long-term, supported by a clear and credible strategy to achieve these.

### Human and labour rights

We believe that how a company manages its human rights strategy is of critical importance to its licence to operate, its impact on people's lives and ultimately its ability to create and preserve long-term holistic value. We endorse and expect companies to align with the UN Guiding Principles on Business and Human Rights (the UNGPs). The UNGPs framework outlines the corporate duty to respect human rights. Companies have a responsibility to disclose and act upon a policy commitment to human rights in their operations and value chains. This includes carrying out human rights due diligence to identify potential and actual human rights impacts; a plan to prevent, mitigate and account for how to address these impacts and providing or cooperating in the provision of remedy if a company has caused or contributed to adverse impacts.

Companies should have a governance structure for human rights which identifies board level oversight and executive accountability. They should report on obligations under the UNGPs, as well as under national legal requirements and relevant international frameworks.

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<sup>26</sup> <http://www.lse.ac.uk/GranthamInstitute/tpi/the-toolkit/>

<sup>27</sup> <https://www.climateaction100.org/progress/net-zero-company-benchmark/>

<sup>28</sup> <https://forest500.org/>

The concept of human rights is simply the universal right to human dignity. However, we acknowledge that human rights strategies and impacts may involve complex and sensitive aspects and seek to engage with companies on these considerations. We may recommend a vote against relevant meeting items, such as re-electing a director, discharging management or approving its reporting if:

- a company is in clear breach of its applicable regulatory responsibilities related to human rights (such as the UK's Modern Slavery Act) or responsibilities outlined in the UNGPs; and/or
- there is sufficient evidence that a company has caused or contributed to egregious, adverse human rights impacts or controversies and has failed to provide appropriate remedy.

### TRANSPARENCY, TAX AND AUDIT

We believe that the quality of narrative reporting reflects the board's strategic thinking, its line of sight into operations and how well it oversees the company. Boards must report openly and transparently on the performance of the company and their stewardship of it over the year, acknowledging the challenges, as well as the achievements, the state of the market and the competitive landscape. It is also fundamental that each company reports in a way that allows investors to understand the main risks that the board has identified for the business, along with how the company manages and mitigates them. This includes environmental, social and governance, as well as financial and strategic, risks.

#### Tax

Companies should recognise the importance of taxation to the funding of public services on which they and their stakeholders rely, and pay their fair contribution. The Covid-19 pandemic has emphasised the importance of companies paying their fair contribution as all businesses have directly or indirectly benefitted from government action to support the economy.

Fair payment of tax, based on the intention of tax law and in proportion to the location of economic value generated, is an important pillar of a company's social licence to operate. We believe that companies that seek to aggressively minimise their tax payments will face increasing reputational and financial risks.

We expect companies to:

- Comply with the intention of tax laws and regulations in all countries of operation.
- Pay taxes in-line with where economic value is generated.
- Publish a global tax policy describing their approach to tax risk, controls and oversight, including any material variations across the entity. This should include policy on corporate structuring in low tax jurisdictions, intra-group transactions and the use of tax incentives from public authorities.

- Ensure their tax policies and practices do not damage their social licence to operate in all jurisdictions in which they have a presence.
- Disclose publicly the full extent of taxes paid or collected by them in each country. Reporting on each country should include the purpose of the local corporate entity along with comparable corporate data such as revenue, profit before tax and number of employees. We recommend use of the GRI reporting standard on tax.
- Ensure they have sufficient oversight of tax policy, risk and controls in board and board committee work.
- Avoid the use or promotion of aggressive tax avoidance strategies either for their corporate taxes or those of employees, contractors or customers.

### Audit

Shareholders in listed companies rely on the quality and robustness of the audited information those companies report to the market when making investment decisions, and when holding company management and boards to account. High quality and effective audits are vital to ensure the markets trust and have confidence in the information companies report.

Audits should provide assurance to shareholders that the financial statements present a prudent, true and fair view of the financial results, cash-flows and financial strength of a company. In recent years, we have seen a spate of business failures following poor quality audits. These high-profile cases have raised questions about the quality, relevance, professionalism and independence of audits and external audit firms, and strengthened calls for reform.

#### Audit committees

Shareholders, regulators and other stakeholders have increasingly focused on the role and performance of audit committees and how they discharge their duties. Beyond the oversight of the financial reporting process and the appointment and oversight of the external auditor, audit committees have important risk and compliance oversight responsibilities, including oversight of internal audit and whistleblowing facilities, as delegated by boards or as specified by laws or regulations. Assignment of substantial non-audit-related oversight mandates to audit committees may be seen as a signal that the audit committee is overburdened, with the risk that duties are being delegated to management. A better course of action may be to set up a further committee of the board to address other material non-audit matters.

#### Auditor rotation

Maintaining independent external assurance is a fundamental pillar of good stewardship and the fiduciary duty of a board of directors. Independence, and potentially audit quality, is at risk when the same assurance provider is maintained for too long – whether the audit partner or audit firm. Only by rotating the audit firm at regular intervals can auditor independence and quality be protected, in the interests of shareholders and other stakeholders. Our view is that auditor rotation can also add value as it welcomes a new firm with a different approach and a new set of subject specialists with a fresh pair of eyes,

fresh challenge and opinions. We wish to see companies establish policies of mandatory rotation of the audit firm after 10 years tenure..

At some Dutch companies, disclosures need to make an informed shareholders' vote at the AGM on the appointment of the external auditor are still under par. As the decision to rotate the audit firm is an important AGM voting item and as we expect more audit firm rotations in the upcoming years (as the legal deadline of 10 years is approaching), we urge all Dutch listed companies to provide more information on the reasons of the proposed rotation and on the tender procedure in the explanatory notes to the AGM agenda. The explanatory notes should at least include the names of the audit firms that were requested to submit a proposal, a description of the selection criteria, a description of the selection process, the decisive reason(s) for the recommendation of the audit firm in question, the scope of the audit assignment and the proposed duration of the audit engagement.

### Non-audit services and fees

As part of overseeing the external auditor, the audit committee must establish and enforce a policy on what non-audit services the company can procure from the external auditor. We pay close attention to these services and related fees to ensure that they do not compromise auditor independence, which could compromise the integrity of the audit. The non-audit fees should normally be substantially lower than the audit fee.

As a guideline, non-audit fees should not exceed 70% of audit fees in any given year<sup>29</sup>. If this is exceeded, there should be a clear explanation as to why it was necessary for the auditor to provide these services (for example, for certain services such as reviewing interim reporting or performing due diligence on transactions) and how the independence and objectivity of the audit was assured. In these cases, we also expect the committee to take action to ensure this does not reoccur, either by tendering for a new audit firm or reallocating non-audit work to a different firm.

We recognise that audit quality cannot be ensured solely through regular rotation of external auditors or reducing conflicts caused by the payment of fees for non-audit work. We expect audit committee chairs and committee members to understand the organisation, challenge management and external and internal audit teams, and to follow best practice guidance when appointing audit firms. Committee chairs and members should ensure they have sufficient time to fulfil their duties, which we expect to be significant, particularly for large, complex organisations.

### Accounting practices

We are concerned that accounting standards, as applied, do not always reflect underlying company performance. We encourage companies to apply accounting standards in a manner which is prudent and provides a true and fair view. Where application of the standards does not provide such a view, we expect companies and their auditors to make this clear to investors.

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<sup>29</sup> [Guidelines on "Monitoring the fee cap of non-audit services" \(europa.eu\)](#)

As such, we expect companies to avoid aggressive accounting practices that represent the company's financial position in a flattering light. This creates a reliance on the most optimistic of outcomes transpiring in subsequent years, which can easily compound up to the point that a preventable collapse finally occurs. We expect companies to recognise liabilities in a timely fashion, and to only realise profits where there is a very high degree of confidence in their quality. We also expect a clear indication of the quality of any unrealised profits found in the company's income statement.

### Audit and climate change

Where material or potentially material we expect companies to disclose climate and other environmental and social matters in its financial statements and clearly discuss the connection between accounting assumptions and the climate change impacts based on alignment to the Paris Agreement. We expect the auditor to communicate climate and other ESG matters as critical audit matters to the audit committee where material and involving challenging, subjective and or complex auditor judgement.

To the extent a company's financial statement does not adequately consider material climate risks and there is no corresponding explanation as to why, we may recommend a vote against the audit committee chair and auditor ratification. For more information on our corporate governance expectations related to climate change, please see the Climate Change section above.

## Federated Hermes

Federated Hermes is a global leader in active, responsible investing.

Guided by our conviction that responsible investing is the best way to create long-term wealth, we provide specialised capabilities across equity, fixed income and private markets, multi-asset and liquidity management strategies, and world-leading stewardship.

Our goals are to help people invest and retire better, to help clients achieve better risk-adjusted returns, and to contribute to positive outcomes that benefit the wider world.

All activities previously carried out by Hermes now form the international business of Federated Hermes. Our brand has evolved, but we still offer the same distinct investment propositions and pioneering responsible investment and stewardship services for which we are renowned – in addition to important new strategies from the entire group.

## Our investment and stewardship capabilities:

- **Active equities:** global and regional
- **Fixed income:** across regions, sectors and the yield curve
- **Liquidity:** solutions driven by four decades of experience
- **Private markets:** real estate, infrastructure, private equity and debt
- **Stewardship:** corporate engagement, proxy voting, policy advocacy

## Why EOS?

EOS enables institutional shareholders around the world to meet their fiduciary responsibilities and become active owners of public companies. EOS is based on the premise that companies with informed and involved shareholders are more likely to achieve superior long-term performance than those without.

For more information, visit [www.hermes-investment.com](http://www.hermes-investment.com) or connect with us on social media:



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