

Response to the ASX Corporate Governance Council's Consultation Paper:

Corporate Governance Principles and Recommendations – 3<sup>rd</sup> Edition

BlackRock, Inc. (BlackRock) welcomes the opportunity to comment on the ASX Corporate Governance Council's (Council) draft third edition of the Corporate Governance Principles and Recommendations (Principles).

BlackRock is committed to engaging with companies and voting proxies in the best long-term economic interests of its clients. Our Corporate Governance and Responsible Investment ("CGRI") team comprises 19 professionals dedicated to proxy voting and company engagement in six offices around the globe. Additionally, approximately 40 senior investment professionals across our global offices oversee and guide the work of the CGRI team. BlackRock votes at approximately 15,000 shareholder meetings annually, across 90 countries, in accordance with our internally-developed proxy voting guidelines. In Australia, BlackRock casts votes in approximately 450 meetings annually. BlackRock reviews the corporate governance practices of the Australian companies in which it invests against its own comprehensive guidelines (attached to this submission).

We are generally supportive of the changes proposed and will therefore only comment on those recommendations that we believe should be modified. These are set out below, with the text highlighted in yellow representing suggested additional/amended text:

Recommendation 1.2

- b) Provide security holders with all material information relevant to a decision on whether or not to elect or re-elect a director, including key information about the particular director's background and the skills and experience that the director brings to the board,

*BlackRock believes it is important for shareholders to understand the a director's background and further what skill set a director brings to the board when assessing whether or not to elect or re-elect such director. We propose that this requirement be part of the actual recommendation rather than the commentary.*

Box 1.5 Suggested additions for the content of a diversity policy

9. A description of the governance structure of the policy i.e. who is accountable for implementation and outcomes;
10. Why the board believes the diversity policy is beneficial to the company, that is, an articulation of a compelling business case for gender diversity in the entity as part of the business strategy, and whether there are internal procedures to review the effectiveness of the diversity policy;
11. Initiatives the company has in place (if any) to address diversity in senior executive positions and whether those initiatives are measured and evaluated; and
12. Any work undertaken or policies on pay equity.

*BlackRock believes the additional disclosures will provide shareholders with a better understanding of how the board manages its diversity policies.*

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## Principle 2 Commentary

### Structure the board to add value

A listed company should have a board of an appropriate size and composition. The directors should be competent, with the skills, experience and commitment to enable them to discharge the duties of the board effectively.

*BlackRock believes that the word “competent” should be included in order to describe a structure that adds value.*

### Commentary

A high performing, effective board is essential for the proper governance of a listed entity. The board needs an appropriate blend of executive and non-executive directors. This includes having a sufficient number of independent non-executive directors who can challenge management and hold them to account, and also represent the best interests of the listed entity and its security holders as a whole rather than those of individual security holders or interest groups. Given the nature of the role it is important that a non-executive director has spare capacity to dedicate to the company in the event of a major development such as a hostile takeover. The demands on non-executive directors increase significantly in such situations and they must have the required time available to fulfil their duties to shareholders. It is the responsibility of the chairman to ensure on a continuing basis that all the directors are able to fulfil their duties, and are participating actively and contributing to the workload of the board. This can be reaffirmed through a formal evaluation each year.

*BlackRock believes the issue of non-executives having sufficient capacity to fulfil their responsibilities, both routinely and in the event extraordinary circumstances arise, is very important to protect shareholders.*

### Box 2.1 – the defining characteristics of an independent director

A director of a listed entity should be characterised and described as an independent director only if he or she is free of any interest, position, association or relationship that might influence, or reasonably be perceived to influence, his or her capacity to bring an independent judgement to bear on issues before the board and to act in the best interests of the entity and its security holders generally.

Examples of interests, positions, associations and relationships that might cause doubts about the independence of a director include if the director:

- is, or has been, employed in an executive capacity by the entity or any of its related entities and there has not been a period of at least three years between ceasing such employment and serving on the board;
- is, or has within the last three years been, a partner, shareholder, director or senior employee of a professional adviser or consultant to the entity or any of its related entities;
- is, or has within the last three years been, a material supplier or customer of the entity or any of its related entities, or an officer of, or otherwise associated directly or indirectly with, such a supplier or customer;
- is a substantial shareholder of the entity or an officer of, or otherwise associated directly or indirectly with, a substantial shareholder of the entity;
- has a contractual relationship with the entity or its related entities other than as a director;
- has close family ties with any person who falls within any of the categories described above; or
- has been a director of the entity for more than 9 years.
- has participated in equity-based remuneration that vests based on performance or continuing service as a non-executive director;
- has business or other relationship which could, or could reasonably be perceived to, materially interfere with the director’s ability to act in the best interests of the company.

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In each case, the **materiality** of the interest, **potential influence**, position, association or relationship needs to be assessed to determine whether it might interfere, or might reasonably be seen to interfere, with the director's capacity to bring an independent judgement to bear on issues before the board and to act in the best interests of the entity and its security holders generally. **Any such interests should be disclosed to the shareholders with sufficient explanation to enable them to determine whether the interest or relationship is likely to affect a director's independence.**

*BlackRock believes that the word "material" should be removed as indicated above to ensure that where a relationship exists and the board believes the non-executive directors is independent, full disclosure of the nature of the relationship and the amounts involved should be disclosed to allow shareholders to judge whether or not they believe the transaction is material or not and if there is potential for the transaction to impair the director's independence.*

*BlackRock also believes that when non-executive directors participate in equity based remuneration that involves performance related or other vesting conditions, their decision making might be, or be perceived to be, biased and their independence compromised.*

## **Recommendation 8.3:**

**A listed entity should:**

**(a) have a "clawback" policy which sets out the circumstances in which the entity may claw back performance-based remuneration from its senior executives;**

**(b) disclose that policy or a summary of it; and**

**(c) disclose as at the end of each reporting period:**

**(1) whether any performance-based remuneration has been clawed back in accordance with the policy during the reporting period; and**

**(2) where performance-based remuneration should have been clawed back in accordance with the policy during the reporting period but was not, the reasons for this.**

## **Commentary**

**Where a senior executive has received performance-based remuneration as a result of the listed entity's financial performance and it is subsequently revealed that its financial statements were materially misstated or some other event has occurred that would mean that the senior executive should not have received some or all of the performance-based remuneration, the listed entity should be able to recoup the excess remuneration paid to the senior executive.**

**To deal with this, a listed entity should have in place a clawback policy (either as a standalone policy or as part of its broader remuneration policy) which sets out the circumstances in which the entity may claw back a senior executive's remuneration and how those amounts will be clawed back (for example, by requiring the senior executive to pay back remuneration, by reducing any earned but as yet unvested incentives, or by adjusting current year incentives or fixed remuneration to take account of the previous overpayment). Generally speaking, a listed entity should include contractual provisions in the service agreements with its senior executives that conform to the clawback policy and facilitate the recoupment of remuneration from the senior executive in accordance with the policy.**

## **Unexpected or unintended remuneration outcomes**

**In the event where outcomes of pay have been unexpected or unintended relative to the performance of the company, the remuneration policy should allow the board to have discretion to adjust downwards and where appropriate eliminate payment of performance based remuneration. Where the board has used its discretion to adjust downwards or eliminate performance based remuneration, the remuneration report should disclose that discretion has been used and explain how and why the discretion was used.**

## **Commentary**

**Where the outcome of performance based pay has been materially misaligned with the performance of a listed entity the remuneration policy should give the board discretion to adjust downwards any unvested**

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component of performance based remuneration and disclose that discretion has been used and explain how and why the discretion was used.

*BlackRock has concerns regarding the proposed wording and the use of the words "claw back". Following release of the "Corporations Legislation Amendment (Remuneration Disclosures and Other Measures) Bill 2012" by Treasury, companies have been including "claw back" policies as part of overall remuneration policy. BlackRock reviewed these policies and found that most related to claw back in the event of a "material misstatement" of financial statements. Further research by BlackRock concluded that "material misstatements" rarely if ever occur. The conclusion reached was that a significant percentage of current claw back policies are ineffective in the event of an unexpected or unintended remuneration outcome. BlackRock recommends that rather than focussing on the word "claw back", the focus should be on the "unexpected or unintended remuneration outcome" and a policy which describes the board's approach to such situations.*

We appreciate the opportunity to provide our views and also commend the Council for undertaking such a comprehensive review of the Principles.

Please feel free to contact the writer should you wish to discuss any of the issues raised in this submission.

Yours sincerely,

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