Our approach to engagement on board quality and effectiveness

BlackRock.

Investment Stewardship

At BlackRock, investment stewardship serves as a link between our clients and the companies they invest in and is one of the ways we fulfill our fiduciary responsibilities as an asset manager to our clients. We do this through engaging with companies to improve our understanding of their business models and material risks and opportunities. We also engage to inform our voting decisions for clients who authorize us to vote on their behalf. Our sole focus when conducting our stewardship program under our Benchmark Policies is to advance our clients' long-term financial interests.[1]

Our investment stewardship efforts have always started with the board and executive leadership. We recognize that accepted standards and norms of corporate governance can differ between markets. However, we believe there are certain fundamental elements of governance practice that are intrinsic globally to a company's ability to create long-term financial value. One of these is a high caliber, effective board responsible for overseeing and advising management and accountable to shareholders.

Board quality and effectiveness as an investment issue

As we explain in the BlackRock Investment Stewardship (BIS) Global Principles, appropriately qualified, engaged directors with characteristics relevant to a company's business enhance the ability of the board to add value and be the voice of shareholders in board discussions. In our view, a strong board gives a company a competitive advantage, providing valuable oversight and contributing to the most important management decisions that support long-term financial performance. This is why our investment stewardship efforts have always started with the performance of the board of directors and why we see engagement with, and the election of, directors as one of our most important responsibilities. The election of directors to the board is a near-universal right of shareholders globally and an important signal of support for, or concern about, the performance of the board in overseeing and advising management.

An effective board has a number of responsibilities, including but not limited to the following:

- Establishing an appropriate corporate governance structure.
- Supporting and overseeing management in setting long-term strategic goals and applicable measures of financial value creation and milestones that will demonstrate progress, and taking steps to address anticipated or actual obstacles to success.
- Providing oversight on the identification and management of material risks and opportunities in a company's business model.
- Overseeing the financial resilience of the company, the integrity of financial statements, and the robustness of the Enterprise Risk Management framework.[2]
- Making decisions on matters that require independent evaluation, which may include mergers and other significant financial transactions.
- Having a formal plan for both anticipated and unplanned leadership succession, including key board roles.
- Establishing and overseeing executive compensation structures that help the company attract, retain, and reward key personnel, while ensuring appropriate risk behaviors, consistent with delivering long-term financial performance.

Clear definitions of the respective roles of the board, the board sub-committees, and senior management contribute to board and governance effectiveness. These responsibilities and structures may differ by company, sector, and geography, as each board tailors its approach to its company's context in light of local regulations and corporate governance norms.[3]

Given the dynamic nature of business, it is beneficial for new directors to be brought onto the board periodically to refresh the group's thinking in a manner that supports both continuity and appropriate succession planning. In our view, this refreshment should include the assessment of factors such as any gaps in skills, experience, and independence. As noted in the BIS Global Principles, we are interested in understanding how a company achieves a variety of experiences, perspectives, and skillsets in the board room. We see it as a means of promoting diversity of thought to avoid "group think" in the board's exercise of its responsibilities to advise and oversee management.

Our approach to engagement on board quality and effectiveness

We take a multifaceted approach towards evaluating board quality and effectiveness. In assessing sound governance, we take into consideration a number of factors, including the sector, market, and business environment within which a company is operating, and how that influences the responsibilities and composition of the board and how it functions.[4]

When evaluating boards as a whole, we look at a number of factors. This includes the board's effectiveness as a group, individual directors' independence and time commitments, as well as the breadth and relevance of director experiences and skillsets, and how these factors may contribute to the financial performance of the company. We look to boards to establish a formal and transparent process for nominating directors that reflects the company's long-term strategy and business model. In our experience, regular director elections benefit boards' ability to adjust their composition in an orderly manner to account for a company's operating environment, and to refresh the group's thinking on matters material to financial value creation.

We engage, as necessary, with members of the board's nominating and/or governance committee to assess whether governance practices and board composition are appropriate given a company's business model and we take into consideration a number of factors, including the sector, market, and business environment within which a company is operating. In our engagements, we may discuss various governance topics, including board composition and independent leadership, board oversight of management's strategy and approach to risk management, succession planning for key board and management roles, and the board's nomination and evaluation processes.

We look to understand the board's views on topics that, in our experience, can demonstrate a robust approach to board quality and effectiveness, including, where appropriate:

- How the board's composition reflects the company's stated strategy, trends impacting the business, the breadth of the company's key stakeholders and succession expectations, and how the board oversees management's strategy and approach to risk management – including of material or business-relevant sustainability-related opportunities and risks.

- How the board integrates the variety of perspectives directors bring to facilitate robust and constructive discussions that result in sound decisions, and whether the board has sub-committees responsible for oversight of key governance matters, e.g., audit oversight or director nominations.

- How the board approaches periodically bringing in new directors, including whether external advisors or search firms are used to identify candidates, the extent to which independence, diversity, skillset, and tenure are considerations, and whether the board uses mechanisms such as a mandatory retirement age or term limit to manage board refreshment.

- How the board considers regional best practices as they relate to governance structure, board composition, and the periodic introduction of new directors to the board.

- How the board evaluates and gains comfort with each director's outside commitments, particularly those to other public company boards.

- How the board assesses independent directors' ability to act in the interests of all shareholders. Generally, this would include directors being free of close affiliations with management, other directors or commercial entities that may impair their independent judgement, significant share ownership, and tenure (including the board's view of the independence of any long-tenured members).

- The board's performance evaluation process, including how it may inform director nominations and management and director succession processes, and how the board develops independent board leadership (including whether committee assignments are rotated on a staggered basis to foster diverse perspectives and enable directors to develop a breadth of knowledge within the board).

NM1224U-4112552-2/3

Endnotes

1. BIS' Benchmark Policies, and the vote decisions made consistent with these policies, take a financial materiality-based approach and are focused solely on advancing clients' financial interests. BIS' Benchmark Policies – comprised of the BIS Global Principles, regional voting guidelines, and engagement priorities – provide clients, companies, and others, guidance on our position on common corporate governance matters. We take a globally consistent approach, while recognizing the unique markets and sectors in which companies operate. Other materials on the BIS website might also provide useful context.
2. Enterprise risk management is a process, effected by the entity's board of directors, management, and other personnel, applied in strategy setting and across the enterprise, designed to identify potential events that may affect the entity, and manage risk to be within the risk appetite, to provide reasonable assurance regarding the achievement of objectives. (Committee of Sponsoring Organizations of the Treadway Commission (COSO), Enterprise Risk Management, 2023. Please see: https://www.coso.org/guidance-erm).
3. For example, in Asia, where concentrated ownership structures are common, it is often the case that controlling shareholders dominate the board even if they have less than majority ownership of the company. We look to companies, through a robust selection process, to nominate non-executive directors who can bring an independent view to and influence on board discussions to help protect minority shareholder interests and the long-term financial value of the company.
4. We recognize that some companies operate across multiple geographies and regulatory regimes, which can result in differing governance and voting polices being applied by their investors. For instance, impediments to director independence may vary, as may thresholds for perceived long-tenure. Additionally, different board structures and responsibilities may influence the demands on directors. We explain in our regional voting guidelines how we assess key board issues such as director independence, tenure limits, election cycles, diversity, and time commitments in the context of local market norms and regulations.

Want to know more?

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