

# **BlackRock Investment Stewardship**

Proxy voting guidelines for Chinese securities  
Effective as of January 2024

# Contents

<b>Executive Summary</b> .....	<b>3</b>
<b>Key themes</b> .....	<b>4</b>
<b>Boards and directors</b> .....	<b>5</b>
<b>Accounts, statutory reports, auditors and audit-related issues</b> .....	<b>11</b>
<b>Capital management</b> .....	<b>12</b>
<b>Capital structure, mergers, asset sales, related-party and other special transactions</b> .....	<b>13</b>
<b>Compensation and benefits</b> .....	<b>16</b>
<b>Material sustainability-related risks and opportunities</b> .....	<b>19</b>
<b>Shareholder proposals</b> .....	<b>21</b>
<b>Other corporate governance matters</b> .....	<b>22</b>
<b>Voting Choice</b> .....	<b>23</b>

These guidelines should be read in conjunction with the BlackRock Investment Stewardship [Global Principles](#). For companies with more than one listing, including a listing outside of China, we expect companies to apply corporate governance practices of the jurisdiction with the highest standards.

## Executive Summary

As part of our fiduciary duty to our clients, we consider it one of our responsibilities to promote sound corporate governance as an informed, engaged shareholder on their behalf. At BlackRock, this is the responsibility of the BlackRock Investment Stewardship (BIS) team.

In our experience, sound governance is critical to the success of a company, the protection of investors' interests, and long-term financial value creation. We have also observed that well-managed companies will effectively evaluate and address risks and opportunities relevant to their businesses, which supports durable, long-term financial value creation. As one of many minority shareholders, BlackRock cannot – and does not try to – direct a company's strategy or its implementation. Rather, we take a constructive, long-term approach with companies and seek to understand how they are managing the drivers of risk and financial value creation in their business models.

Our policies for China are based on the Company Law, Securities Law, Listing Rules of Shanghai and Shenzhen Stock Exchange, and the Code of Corporate Governance promulgated by the China Securities Regulatory Commission (the CSRC) and other relevant guidelines such as the Measures for the Administration of Independent Directors of Listed Companies<sup>1</sup>, established also by the CSRC. These all have in common the principles of accountability, transparency, fairness and responsibility.

Our approach to voting and corporate engagement is also informed by guidance on exercising ownership responsibilities issued by organizations such as the United Nations (the Principles of Responsible Investment) and the International Corporate Governance Network. We are actively involved in these and a number of other regional and global organizations and believe our principles are consistent with their guidance.

### “Comply or explain” approach

The Code of Corporate Governance is implemented on a comply-or-explain basis. Companies are allowed to not adopt recommended practices as long as a cogent explanation has been provided for non-compliance with the particular practice. BlackRock expects companies that do not follow recommended practices to provide explicit justification of any deviation by explaining how these serve the interests of the company's shareholders.

### Shareholder rights

We believe that there are certain fundamental rights attached to shareholding. Shareholders should have the right to:

- Elect, remove, and nominate directors, approve the appointment of the auditor, and amend the corporate charter or by-laws.
- Vote on key board decisions that are material to the protection of their investment, including but not limited to, changes to the purpose of the business, dilution levels and pre-emptive rights, and the distribution of income and capital structure.

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<sup>1</sup> [China Securities Regulatory Commission](#).

- Access sufficient and timely information on material governance, strategic, and business matters to make informed decisions.

In our view, shareholder voting rights should be proportionate to economic ownership—the principle of “one share, one vote” helps to achieve this balance.

Consistent with these shareholder rights, BlackRock monitors and provides feedback to companies in our role as stewards of our clients’ assets. Investment stewardship is how we use our voice as an investor to promote sound corporate governance and business practices that support the ability of companies to deliver long-term financial performance for our clients. We do this through engagement with companies, proxy voting on behalf of those clients who have given us authority, and participating in market-level dialogue to improve corporate governance standards.

Engagement is an important mechanism for providing feedback on company practices and disclosures, particularly where we believe they could be enhanced to support a company’s ability to deliver financial performance. Similarly, it provides us with an opportunity to hear directly from company boards and management on how they believe their actions are aligned with the long-term economic interests of shareholders. Engagement with companies may also inform our proxy voting decisions.

As a fiduciary, we vote in the long-term economic interests of our clients. Generally, we support the recommendations of the board of directors and management. However, there may be instances where we vote against the re-election of directors or other management proposals, or support shareholder proposals. For instance, we may vote against management recommendations where we are concerned that the board may not be acting in the long-term economic interests of shareholders, or disclosures do not provide sufficient information to assess how material, strategic risks and opportunities have been managed.

## Key themes

These guidelines will be used to assist BlackRock in assessing proposals presented at shareholder meetings. When assessing any proposal put to shareholders, BlackRock takes into account the unique circumstances of the relevant company and our assessment of the impact of such a proposal on the sustainable growth of the company. We aim to engage with management or members of the board, as appropriate, on contentious and high profile issues before determining how to vote.

These guidelines are divided into nine key themes as follows:

- Boards and directors;
- Accounts, statutory reports, auditors and audit-related issues;
- Capital management;
- Capital structure, mergers, asset sales, related-party and other special transactions;
- Compensation and benefits;
- Material sustainability-related risks and opportunities;
- Shareholder proposals
- Other corporate governance matters;

- Voting Choice

## **Boards and directors**

The board should establish and maintain a framework of robust and effective governance mechanisms to support its oversight of the company's strategy and operations consistent with the long-term economic interests of investors. There should be clear descriptions of the role of the board and the committees of the board and how directors engage with and oversee management. We look to the board to articulate the effectiveness of these mechanisms in overseeing the management of business risks and opportunities and the fulfillment of the company's purpose and strategy.

Where a company has not adequately disclosed and demonstrated that its board has fulfilled these corporate governance and risk oversight responsibilities, we will consider voting against the election of directors who, on our assessment, have particular responsibility for the issues. We assess director performance on a case-by-case basis and in light of each company's circumstances, taking into consideration our assessment of their governance, business practices that support durable, long-term value creation, and performance. Set out below are ways in which boards and directors can demonstrate a commitment to acting in the long-term economic interests of all shareholders.

### **Regular accountability**

It is our view that directors should stand for election on a regular basis, ideally annually. In our experience, annual director elections allow shareholders to reaffirm their support for board members and/or hold them accountable for their decisions in a timely manner. When board members are not elected annually, in our view, it is good practice for boards to have a rotation policy to ensure that, through a board cycle, all directors have had their appointment re-confirmed, with a proportion of directors being put forward for election at each annual general meeting.

### **Effective board composition**

Regular director elections also give boards the opportunity to adjust their composition in an orderly way to reflect developments in the company's strategy and the market environment. In our view, it is beneficial for new directors to be brought onto the board periodically to refresh the group's thinking while supporting both continuity and appropriate succession planning. We consider the average overall tenure of the board, and seek a balance between the knowledge and experience of longer-serving directors and the fresh perspectives of directors who joined more recently.

We encourage companies to keep under regular review the effectiveness of their board (including its size), and assess directors nominated for election in the context of the composition of the board as a whole. This assessment should consider a number of factors, including each director's independence and time commitments, as well as the diversity and relevance of director experiences and skillsets, and how these factors may contribute to the performance of the company.

We believe that directors are in the best position to assess the composition and optimal size of the board, but we would be concerned if a board seemed too small to have an appropriate balance of directors or too large to be effective.

We expect the board to establish a robust process to evaluate the performance of the board as a whole and the contributions of each director. BlackRock believes that annual performance reviews of directors and the board contribute to a more efficiently functioning board.

## **Board independence**

At a minimum we believe independent directors should comprise at least one-third of the board for these directors to represent an effective voice. Ideally, a board should consist of a majority of independent directors.

In cases where the board is not at least one third independent and where no explanation has been provided, BlackRock may consider voting against the re-election of the chair of the nomination committee, members of the nomination committee, and/or the chair of the board.

## **Assessment of independence**

In our view, there should be a sufficient number of independent directors, free from conflicts of interest or undue influence from connected parties, to ensure objectivity in the decision-making of the board and their ability to oversee management. Common impediments to independence may include but are not limited to:

- Current or recent employment at the company or a subsidiary
- Being, or representing, a shareholder with a substantial shareholding in the company
- Having any other interest, business, or other relationship which could, or could reasonably be perceived to, materially interfere with a director's ability to act in the best interests of the company and shareholders
- An immediate family member of any of the aforementioned
- Interlocking directorships

## **Conflicts of interest**

BlackRock believes that all independent directors should be free from conflicts of interest. Independent directors, their immediate family or their affiliated companies, who or which engage in material transactions with a company, could be placed in a position where they have to make decisions that may place their interests against those of the shareholders they represent. BlackRock may vote against the election/re-election of a director where an identified conflict of interest may pose a significant and unnecessary risk to shareholders. All potential conflicts of interest should be declared prior to appointment and at each board meeting in relation to any specific agenda items.

## **Independent board leadership**

In our experience, boards are most effective at overseeing and advising management when there is a senior, independent board leader. This director may chair the board, or, where the chair is also the CEO (or is otherwise not independent), be designated as a lead independent director. The role of this director is to enhance the effectiveness of the independent members of the board through shaping the agenda, ensuring adequate information is provided to the board, and encouraging independent director participation in board deliberations. The lead independent director or another appropriate director should be available to meet with shareholders in those situations where an independent director is best placed to explain and contextualize a company's approach.

## **Length of service**

BlackRock believes that shareholders are best served when there is orderly renewal of the board. This should result in directors with accumulated experience while at the same time introduce fresh minds and

experience to the board as well as provide adequate succession planning. An effective renewal process will ensure independent directors do not serve for such lengths of time that their independence may be impaired, although this is not a severe concern in China because the CSRC has a guiding opinion which caps the tenure of independent directors at six years.

BlackRock may consider voting against the re-election of directors who have been on the board for a significant period of time and especially if there is no evidence of board renewal.

## Diversity

We see diversity as a means to promoting diversity of thought and avoiding “group think” in the board’s exercise of its responsibilities to advise and oversee management. It allows boards to have deeper discussions and make more resilient decisions. We ask boards to disclose how diversity is considered in board composition, including professional characteristics, such as a director’s industry experience, specialist areas of expertise and geographic location; as well as demographic characteristics such as gender, race/ethnicity and age. We encourage boards to aspire to meaningful diversity of membership, while recognizing that building a strong, diverse board can take time.

Significant progress has been made in recent years towards advancing gender diversity in the boardroom, following voluntary initiatives and mandatory quotas in markets. The State Council of the People’s Republic of China issued a notice regarding the development of women and children in September 2021<sup>2</sup>, stating an expectation for female representation at companies’ boards and management to increase. A coalition of investment firms advocating for increasing female representation at companies’ boards to 20% by 2025 was also established at a forum in Shenzhen in December 2020.<sup>3</sup>

We generally would not consider single gender boards as diverse boards, and we expect large companies in China<sup>4</sup> to have at least one female board director. In the absence of such, we may vote against the re-election of director(s) responsible for the lack of female representation on such boards.

## Nomination procedure

The company should have a formal and transparent procedure for the appointment and re-appointment of directors. The board should adopt a procedure that can ensure a diverse range of candidates to be considered. Such procedure may involve the engagement of an external professional search firm.

When nominating new directors to the board, we look to companies to provide sufficient information on the individual candidates so that shareholders can assess the suitability of each individual nominee and the overall board composition. These disclosures should give an understanding of how the collective experience and expertise of the board aligns with the company’s long-term strategy and business model. Highly qualified, engaged directors with professional 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 provides a competitive advantage to a company, providing valuable oversight and contributing to the most important management decisions that support long-term financial performance.

The procedure for the nomination and evaluation of the board should be disclosed in the corporate governance section in the annual report. We seek information to understand how the board composition reflects the company’s stated strategy, trends impacting the business and succession expectations.

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<sup>2</sup> [Notice](#) from the State Council regarding the development of women and children, 8 Sep 2021.

<sup>3</sup> First ever [investment coalition](#) advocating for female directors established in Shenzhen, 1 Dec 2020.

<sup>4</sup> Companies in scope would include those listed in Hong Kong as well as constituents of key indices such as CSI 100.

Where this information is not provided, we may consider voting against re-election of members on the nomination committee.

## **Disclosure of director information**

BlackRock expects the following information to be disclosed in the annual report and company website, and the meeting circular when a director is seeking election/re-election:

- Directors' full name and age
- Date appointed to the board (in the case of re-election)
- Brief biography detailing the directors' educational background, working experience, and any other board positions held
- Specific discussion on the skills and experience the director is expected to contribute to the board
- The company's assessment of the director's independence including details of any current dealings with the company

Particularly when a director is seeking election/re-election it is imperative the above information is provided to allow us to determine whether to support the appointment. Where this information is not forthcoming, BlackRock may consider voting against the election/re-election of that director.

## **Sufficient capacity**

As the role and expectations of a director are increasingly demanding, directors must be able to commit an appropriate amount of time to board and committee matters. It is important that directors have the capacity to meet all of their responsibilities – including when there are unforeseen events – and therefore, they should not take on an excessive number of roles that would impair their ability to fulfill their duties.

BlackRock expects companies to provide a clear explanation of the capacity to contribute in situations where a board candidate is a director serving on more than six public company boards. When looking at the number of board mandates, BlackRock will consider if the board memberships are of listed companies in the same group and/or for similar sectors.

BlackRock may vote against the election/re-election of a director where there is a risk the director may be over-committed in respect of other responsibilities and/or commitments (taking into account outside employments and/or board mandates on private companies/investment trusts/foundations). In the case of an executive officer, we would vote against his/her election/re-election only at external boards.

BlackRock may vote against the election of an outside executive as the chairman of the board as we expect the chairman to have more time availability than other non-executive board members. We expect the company to explain why it is necessary for an external executive to lead the board of directors.

## **Meeting attendance**

Although not required<sup>5</sup>, BlackRock believes a listed company should make full disclosure of the attendance of all directors at board and relevant committee meetings in the annual report because this is an important indicator of whether directors are discharging their duties to shareholders effectively.

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<sup>5</sup> Chinese companies are only required to disclose the meeting attendance record of independent directors at board meetings in the annual report.

Directors should ensure they attend all board and relevant committee meetings. BlackRock will consider voting against a director who attends fewer than 75% of board and relevant committee meetings for the past term of being a director, unless compelling reasons for the absenteeism have been disclosed. However, BlackRock will disregard attendance in the first year following appointment as the director may have had commitments made prior to joining the board.

## **Committees**

Appropriately structured board committees provide an efficient mechanism which allows the board to focus on key issues such as audit, board renewal, compensation, risk and any other issues deemed important. Board committees can also provide an important role dealing with conflicts of interests.

BlackRock expects all companies to establish an audit committee and encourages all companies to establish nomination and compensation committees. All committees should have written terms of reference which should, inter alia, clearly set out the committee's roles and responsibilities, composition, structure, membership requirements and the procedures for inviting non-committee members to attend meetings. All committee terms of reference should be available to investors.

All committees should be given the power and resources to meet their obligations under the terms of reference. This will include the right of access to management and the ability to select service providers and advisors at a reasonable cost to the company.

The chairman of a committee should be independent. It is preferable for the chairman of the board not to chair board committees as this may lead to a concentration of power in a single director.

BlackRock expects all companies to disclose whether the key committees are established, and if so, the composition of the key committees, the frequency of committee meetings, and the attendance record of each member on the committee.

## **Audit committee**

The audit committee should comprise only non-executive directors and a majority of independent directors, an independent chair and at least one independent director having appropriate accounting or related financial background.

The terms of reference for the audit committee should have appropriate powers to determine the scope of the audit process, review the effectiveness of the external auditor, assess, review and authorise non-audit work, have access to the internal audit process and to make recommendations regarding the appointment and removal of the external auditor.

Where a risk committee has been established in addition to an audit committee, clear disclosure needs to be made on the responsibilities of each committee and how they interact.

BlackRock generally does not support the election of an executive director on to the audit committee. Where the audit committee does not comprise a majority of independent directors or the chair is not independent, BlackRock will consider voting against the election of the non-independent members of the audit committee particularly if there are other corporate governance issues. Further, where there is evidence showing failure of the audit committee relating to the preparation of financial statements, fraud and general accountability to shareholders, we will consider voting against the re-election of members of the audit committee.

## Compensation committee

The compensation committee should comprise a majority of independent directors and have an independent chair. The responsibilities of the compensation committee should include a review of and recommendations to the board on issues including but not limited to:

- The company's compensation, recruitment, retention and termination policies for senior executives;
- Executive director and senior executives fixed and performance-based compensation to ensure that executives are motivated to pursue the long-term growth and success of the company; and
- The compensation framework for non-executive directors

Where BlackRock believes the compensation committee has failed in its role, we will consider voting against the re-election of the chair/members of the committee.

## Nomination committee

The nomination committee should comprise a majority of independent directors and have an independent chair. The responsibilities of the nomination committee should include a review of and recommendations to the board on issues including but not limited to:

- Assessing the competencies of all directors to ensure the board has an appropriate range of skills and expertise;
- Implementing a plan for identifying, assessing and enhancing director competencies;
- Reviewing, at least annually, the succession plans of the board;
- Ensuring the size and composition of the board is conducive to making appropriate decisions;
- Reviewing the time required of each non-executive director to undertake their role and whether non-executive directors are meeting that requirement;
- Ensuring a process for the evaluation of the performance of the board, its committees and directors and reporting the process to shareholders in the corporate governance report in the annual report;
- The appointment and re-election of directors; and
- Maintaining a watching brief on the development of management and potential for senior executive succession planning from the level below senior executives

Circumstances where BlackRock may consider voting against the re-election of the chair and/or members of the nomination committee include but are not limited to:

- If the composition of the board continues to reflect poor succession planning, renewal or other composition deficiency;
- If the committee approved the nomination or re-election of an individual who has demonstrated a lack of integrity or inability to represent the interests of shareholders or who has an actual or perceived material conflict of interest that poses a risk to shareholders; or
- If the committee fails to hold a meeting in the reporting year.

## **Risk oversight**

Companies should have an established process for identifying, monitoring, and managing key risks. Independent directors should have ready access to relevant management information and outside advice, as appropriate, to ensure they can properly oversee risk management. We encourage companies to provide transparency around risk measurement, mitigation, and reporting to the board. We are particularly interested in understanding how risk oversight processes evolve in response to changes in corporate strategy and / or shifts in the business and related risk environment. Comprehensive disclosure provides investors with a sense of the company's long-term operational risk management practices and, more broadly, the quality of the board's oversight. In the absence of robust disclosures, we may reasonably conclude that companies are not adequately managing risk.

## **Supervisory board**

China has adopted a two-tier structure of board governance. In addition to the board of directors, there is also a supervisory board. According to the Company Law of the People's Republic of China, the supervisory board is authorized to check the financial affairs of the company and to ensure that board directors and senior managers have fulfilled their obligation of fidelity and diligence; and when they have not, propose to remove a director or senior manager and demand rectifications.<sup>6</sup>

The supervisory board must have a minimum of three members, comprising shareholder and employee representatives. No less than one third of members are required to be employee representatives. The supervisory board should be independent of the board of directors, and thus, directors, managers, and financial officers should not be supervisors. BlackRock will generally support the re-election of members of supervisory boards where the structure of the supervisory board meets the legal requirement. However, BlackRock will consider voting against the election of a supervisory board member where we have concerns regarding the performance of the candidate or when the candidate has a relationship with the external audit firm.

## **Accounts, statutory reports, auditors and audit-related issues**

### **Accounts and statutory reports**

BlackRock recognizes the critical importance of financial statements, which should provide a true and fair picture of a company's financial condition. Accordingly, the assumptions made by management and reviewed by the auditor in preparing the financial statements should be reasonable and justified.

Audit committees or equivalent play a vital role in a company's financial reporting system. We hold the members of the audit committee or equivalent responsible for overseeing the management of the audit function. Audit committees or equivalent should have clearly articulated charters that set out the committee's responsibilities and have a rotation plan in place that allows for a periodic refreshment of the committee memberships. We recognize that audit committees will rely on management, internal audit and the independent auditor in fulfilling their responsibilities but look to committee members to demonstrate they have relevant expertise to monitor and oversee the audit process and related activities.

We take particular note of unexplained changes in reporting methodology, cases involving significant financial restatements or ad hoc notifications of material financial weakness. In this respect, audit

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<sup>6</sup> Article 54 of the Company Law of the People's Republic of China.

committees should provide timely disclosure on the remediation of Key and Critical Audit Matters identified either by the external auditor or internal audit function.

The integrity of financial statements depends on the auditor being free of any impediments to being an effective check on management. To that end, it is important that auditors are, and are seen to be, independent. Where an audit firm provides services to the company in addition to the audit, the fees earned should be disclosed and explained. Audit committees should have in place a procedure for assessing annually the independence of the auditor and the quality of the external audit process.

Comprehensive disclosure provides investors with a sense of the company's long-term operational risk management practices and, more broadly, the quality of the board's oversight. The audit or risk committee should periodically review the company's risk assessment and risk management policies and the significant risks and exposures identified by management, the internal auditors or the independent auditors, and management's steps to address them. In the absence of detailed disclosures, we may reasonably conclude that companies are not adequately managing risk.

## **Auditors and audit-related issues**

The appointment of the auditor and the auditor's compensation needs to be reviewed and approved by shareholders on an annual basis. BlackRock expects the audit firms to be well qualified to undertake the task on behalf of shareholders. When a listed company proposes to appoint a different audit firm, BlackRock expects the company to provide a reasonable explanation for changing its audit firm, assuring shareholders that there are no disputes with company management connected with the auditor ceasing to hold office. If significant concerns about issues such as the integrity of the financial statements or the auditors are identified, where no explanation is provided, BlackRock may consider voting against the appointment of a new audit firm or (re-)appointment of the interim auditor and against the re-election of members on the audit committee, especially if the change of auditor has not been brought up for shareholders' vote in the first place.

## **Capital management**

### **Allocation of profits/dividends**

In China, companies are required to submit to shareholders for approval the allocation of income. These proposals are generally not contentious and are supportable. However, where dividend payout ratios appear, without explanation, to be too high or too low BlackRock may consider voting against relevant individuals on the board.

### **Issuance of equities and equity-linked securities**

The issuance of equities and equity-linked securities such as convertible bonds require the approval of shareholders. Further, companies are required to provide detailed information around the issue manner, size, price, places if it is a private placement, and the intended usage of the raised proceeds.

BlackRock reviews such equity financing requests on a case by case basis where the key considerations include the effect of ownership and earnings dilution to existing shareholders, the company's current capital structure, the intended usage of planned proceeds and how it aligns with the company's business development strategy, and the rationale of why other financing methods are not explored. BlackRock generally does not support the issuance of new shares to a controlling shareholder at a deep discount unless a cogent explanation is provided.

## **Issuance of debt instruments**

The issuance of debt instruments such as corporate bonds, short-term and mid-term notes also requires approval from shareholders. The amount of outstanding debt instruments after issuance is capped at 40% of the last audited net asset value of the company.

BlackRock's view is that the board and management is in the best position to decide how to best utilize their debt capacity and optimize their capital structure. Moreover, the CSRC has stringent requirements on the profitability and credit rating of companies applying for debt issuance. Because of the tight regulatory environment, BlackRock does not view such proposals to be problematic and generally votes in favor.

## **Application of bank credit lines**

Chinese companies routinely ask for shareholder approval at the annual general meeting for the proposed aggregate credit lines from commercial banks during the year. We view this is purely a commercial activity and best left with the board and management. BlackRock generally votes in favor of such proposals.

## **Provision of loan guarantees**

Chinese companies routinely provide loan guarantees to subsidiaries and associates (and joint ventures), and sometimes affiliates and unrelated parties. When the cumulative amount of such guaranteed provision exceeds a certain threshold as prescribed in details by the Listing Rules of the Shanghai and Shenzhen Stock Exchange, shareholder approval is required for any subsequent guarantee provision.

BlackRock generally supports the provision of loan guarantees to subsidiaries. We also support the guarantee provision to associates (and joint ventures) if the guarantee provision is proportionate to the company's equity stake in the associates. We generally do not support the provision of loan guarantees to affiliates, particularly a controlling shareholder, or unrelated parties unless a cogent explanation is provided.

## **Provision of loans**

Companies at times propose to provide loans, often termed financial assistance, to subsidiaries and associates, and sometimes affiliates and unrelated parties. These loan provisions need to be approved by shareholders.

BlackRock generally supports the provision of loans to subsidiaries. We also support the loan provision to associates (and joint ventures) if the loan provision is proportionate to the company's equity stake in the associates. We generally do not support the provision of loans to affiliates, particularly a controlling shareholder, or unrelated parties unless a cogent explanation is provided.

## **Capital structure, mergers, asset sales, related-party and other special transactions**

The capital structure of a company is critical to shareholders as it impacts the value of their investment and the priority of their interest in the company relative to that of other equity or debt investors. Pre-emptive rights are a key protection for shareholders against the dilution of their interests.

## Dual class shares

Effective voting rights are basic rights of share ownership and a core principle of effective governance. Shareholders, as the residual claimants, have the strongest interest in protecting company value, and voting rights should match economic exposure, i.e. one share, one vote.

In principle, we disagree with the creation of a share class with equivalent economic exposure and preferential, differentiated voting rights. In our view, this structure violates the fundamental corporate governance principle of proportionality, and results in a concentration of power in the hands of a few shareholders, thus disenfranchising other shareholders and amplifying any potential conflicts of interest. However, we recognize that in certain markets, at least for a period of time, companies may have a valid argument for listing dual classes of shares with differentiated voting rights. In our view, such companies should review these share class structures on a regular basis or as company circumstances change. Additionally, they should seek shareholder approval of their capital structure on a periodic basis via a management proposal at the company's shareholder meeting. The proposal should give unaffiliated shareholders the opportunity to affirm the current structure or establish mechanisms to end or phase out controlling structures at the appropriate time, while minimizing costs to shareholders.

As always, independent directors are expected to protect the interests of all shareholders and BlackRock will potentially vote against re-election of independent directors in companies with dual class share structures if valid concerns arise relating to the economic interests of unaffiliated shareholders being compromised.

## Mergers, asset sales, and other special transactions

In assessing mergers, asset sales, or other special transactions, BlackRock's primary consideration is the long-term economic interests of our clients as shareholders. Boards proposing a transaction should clearly explain the economic and strategic rationale behind it. We will review a proposed transaction to determine the degree to which it can enhance long-term shareholder value. We find long-term investors like our clients typically benefit when proposed transactions have the unanimous support of the board and have been negotiated at arm's length. We may seek reassurance from the board that the financial interests of executives and/or board members in a given transaction have not adversely affected their ability to place shareholders' interests before their own.

We closely examine certain salient features in our analyses. For mergers and asset sales, we assess the degree to which the proposed transaction represents a premium to the company's trading price. In order to filter out the effects of pre-merger news leaks on the parties' share prices, we consider the share price over multiple time periods prior to the date of the merger announcement. In most cases, business combinations should provide a premium. We may consider comparable transaction analyses provided by the parties' financial advisors and our own valuation assessments. For companies facing insolvency or bankruptcy, a premium may not apply. Where the transaction involves related parties, we expect the board to establish a committee comprised of independent directors to review the transaction and report to shareholders. There needs to be a clear favorable business reason for any such transaction.

## Related-party transactions

Related-party transactions (RPTs) are common at Chinese listed companies. These are transactions between the company and their related-parties, as defined in details in the Listing Rules of the Shanghai and Shenzhen Stock Exchange. According to the materiality of the transaction, it may need to be disclosed or submitted to a shareholder meeting for approval. Any shareholder who has a material

interest in the transaction must abstain from voting on the resolution. All related-party transactions need to be vetted by independent directors.

Broadly speaking, there are two types of related-party transactions: 1) one-off transactions, typically asset purchases or disposals; 2) recurring RPTs that are within the ordinary course of business, usually in the form of an ongoing goods and services purchase and provision agreement.

BlackRock assesses one-off RPTs on a case-by-case basis. Key factors we take into consideration include the strategic rationale and the fairness of the transaction terms. Moreover, BlackRock expects the company to disclose in detail the decision-making process the board has gone through and the process the independent directors have gone through to arrive at their recommendation to minority shareholders. For such non-recurring transactions between related parties, the recommendation to support should come from the independent directors, and ideally, the terms should have been assessed through an independent appraisal process. In addition, it is good practice that it be approved by a separate vote of the non-conflicted shareholders. Where the above information is not disclosed or action is not taken to protect the rights of independent shareholders, BlackRock will consider voting against such proposals.

Recurring RPTs involving the purchase and provision of goods and non-financial services are disclosed in the annual report in details and are subject to annual approval by shareholders. In most cases, these transactions are within the normal course of business and are transacted at arms-length terms. Where disclosure is sufficient, BlackRock generally finds these proposals supportable.

## **Financial services agreements**

It is common among Chinese State-Owned Enterprises (SOEs) to establish a finance company within the business group (hereinafter referred to as Group Finance Companies (GFCs)). GFCs are set up to provide a range of financial services (mainly deposit, loan and settlement related) to the group member companies. The main purpose is to better utilize capital within the same group by channeling funds among members through the GFC as companies are banned from directly borrowing from or lending to another corporate entity. GFCs are typically majority owned by the unlisted group parent, which also controls the listed company. A listed company obtains services from a GFC by entering into a financial service agreement, which requires shareholder approval once every three years.

BlackRock recognizes the merits of dealing with a GFC compared to a commercial bank, such as preferential deposit and loan interest rate, and expedited and customized settlement services. However, we are concerned with certain risk aspects unique to dealing with GFCs. While GFCs are subject to the same capital requirements and are also monitored by the China Banking and Insurance Regulatory Commission (CBIRC), as a private entity there is not the same level of transparency compared to large commercial banks, the majority of which are listed. Another key difference is that a GFC only deals with member companies within the same group whilst a commercial bank deals with all participants in the economy. As a result, GFCs are exposed to risks concentrated in a business group while a commercial bank's risk is much more diversified. Moreover, transactions with GFCs are related-party transactions and therefore exposed to conflicts of interest. An extreme example of such conflicts left unchecked is a listed company being exploited by the group as a window of financing given their access to the wider capital market.

It is our view that companies can mitigate these risks by establishing a robust internal review and audit process to ensure each deposit at and loan from the GFC is has a sound business and capital management rationale. Companies should also aim to achieve a level of transparency beyond the minimum requirement around transactions with GFCs and GFCs themselves. Where the GFC is not controlled by a listed company, we have concerns when outstanding deposits at the GFC are consistently

higher than outstanding loans from the GFC. BlackRock may consider voting in favor of a financial services agreement if in our assessment a company has set up an effective risk management mechanism in place to address the conflict of interest, and has disclosed sufficient information about the GFC and the transactions with it. Relevant information includes but is not limited to:

- Historical and expected scale of transactions, especially loans and deposits, with the GFC, even if some of these transactions are not subject to shareholder approval;
- Rationale behind the deposit and loan limit requested;
- Decision-making process of placing deposits and obtaining loans from the GFC;
- Key financial metrics of the GFC such as loan to deposit rate, capital adequacy ratio, amount of non-performing loan;
- Activities other than taking deposits and making loans that the GFC may engage such as equity investments, entrust loans, and finance leasing;
- Interest rates paid on deposits and charged for loans by deposit and loan type;
- The corporate governance structure of the GFC and its loan approving process;
- Percentage of the company's capital deposited at the GFC versus that at a commercial bank; and
- Whether an offsetting mechanism is in place

BlackRock expects such disclosure to be made not only in the meeting circular when shareholder approval is being sought once every three years but also in the annual report so that investors get to review these transactions and the financial strength of the GFC on an annual basis.

## Compensation and benefits

The key purpose of compensation is to reward, attract and retain competent directors, executives and other staff who are fundamental to the long-term sustainable growth of shareholder value, with reward for executives contingent on controllable outcomes that add value.

One of the most important roles of a company's board of directors is to put in place a compensation structure that incentivizes and rewards executives appropriately. There should be a clear link between variable pay and a company's operational and financial performance. Performance metrics should be stretching and aligned with a company's strategy and business model. BIS does not have a position on the use of sustainability-related criteria in compensation structures, but in our view, where companies choose to include these components, they should be adequately disclosed, material to the company's strategy, and as rigorous as other financial or operational targets. Long-term incentive plans should encompass timeframes that 1) are distinct from annual executive compensation structures and metrics, and 2) encourage the delivery of strong financial results over a period of years. Compensation committee should guard against contractual arrangements that would entitle executives to material compensation for early termination of their employment.

We are not supportive of one-off or special bonuses unrelated to company or individual performance. Where discretion has been used by the compensation committee or its equivalent, we expect disclosure relating to how and why the discretion was used, and how the adjusted outcome is aligned with the interests of shareholders. We acknowledge that the use of peer group evaluation by compensation

committees can help ensure competitive pay; however, we are concerned when the rationale for increases in total compensation at a company is solely based on peer benchmarking rather than a rigorous measure of outperformance. We encourage companies to clearly explain how compensation outcomes have rewarded performance.

We encourage boards to consider building clawback provisions into incentive plans such that companies could clawback compensation or require executives to forgo awards when compensation was based on faulty financial statements or deceptive business practices. We also favor recoupment from or the foregoing of the grant of any awards by any senior executive whose behavior caused material financial harm to shareholders, material reputational risk to the company, or resulted in a criminal investigation, even if such actions did not ultimately result in a material restatement of past results.

The level of director and executive compensation is generally not excessive at Chinese companies. However, compensation is only disclosed as a lump-sum number for each director and senior executive in the annual report, without a breakdown of the pay components such as base salary, performance bonus, and benefits. This provides little transparency around the compensation structure of directors and senior executives, and therefore leaves investors incapable of learning whether senior executives are properly incentivised to manage the company in a way that is in the long-term interest of shareholders.

BlackRock expects companies to disclose the compensation paid to each director and senior executive and the breakdown of the payment. Where there is performance-based pay, companies should also disclose the key performance metrics selected and the rationale for their inclusion, e.g. why these metrics are suitable considering the company's development stage, business strategy, and the nature of the industry the company is in.

We use third party research, in addition to our own analysis, to evaluate existing and proposed compensation structures. We may vote against members of the compensation committee or equivalent board members for poor compensation practices or structures.

## **Independent director compensation**

The role of the independent director is to monitor the strategy, performance and compensation of the executives and to protect the interests of shareholders. Sufficient compensation should be provided to attract and retain suitably qualified independent directors and encourage them to undertake their role diligently. The executive arm and any major shareholder should not have any undue influence over the compensation of independent directors.

Independent director compensation should be structured in such a way that it aligns the interests of the directors with those of the shareholders they represent. The structure of independent director compensation should not provide any disincentive to resign from the board should an issue of conflict or any other issue that would impair a director's independence arise.

Independent directors should receive a fixed annual fee, including additional fixed fees for board committee membership for their services. BlackRock supports independent directors entering into "salary sacrifice" arrangements whereby a portion of their fees is received by way of fully paid shares purchased on market.

BlackRock does not generally support the granting of options to independent directors as such securities do not have the same risk profile as the ordinary shares held by ordinary shareholders and therefore may not align the interests of directors with those shareholders they represent. Independent directors should not receive performance-based compensation as to do so would more closely align their interests with those of management, whose performance and compensation they are intended to monitor on behalf of

shareholders. Where options or performance-based compensation have been granted to independent directors, BlackRock will consider voting against any such proposals and the re-election of the chair of the compensation committee.

## **Equity-based incentive plan**

### **Stock option/Restricted stock scheme**

It is becoming increasingly common among Chinese companies to establish a stock option/restricted stock scheme to incentivise and retain key employees. Such schemes typically require approval which is valid for three to five years after which further shareholder approval is required or another plan is put to shareholder vote.

According to the CSRC, companies may select performance metrics that measures their value creation for shareholders such as return on equity, earnings per share, and dividend per share, or metric that indicate the company's profitability and growth such as the growth rate of net profit and revenue. The company can either choose to use their peer performance or historical performance as the benchmark. Another regulatory feature of these plans is that the total number of shares underlying all the outstanding equity-based compensation schemes shall be capped at 10% of the total amount of equity issued for mainboard-listed companies and 20% for ChiNext or STAR board listed companies.

Disclosure around such plans is fairly comprehensive. Companies are required to disclose the full list of plan participants, number of stock options/restricted stocks to be issued to each participant, exercise price of the stock option, issue price of the restricted stocks, grant schedule, and company performance measures and hurdles. Independent directors and non-employee representative supervisors are excluded from these plans.

Many Chinese companies do not have compensation committees, as a result such plans are administered by the whole board, which may include participants in the plan. Given the regulatory restrictions on issuances, and the comprehensive nature of disclosure, we will support such plans as long as the overall dilution is considered reasonable and justified, despite plan participants also being members of the board.

### **Employee stock participation plan**

Starting from June 2014, companies can also establish employee stock participation plans (ESPPs) which aim to increase employee ownership in the company for better alignment of the interests of employees with shareholders. There is a minimum retention period of 12 months if stocks are purchased from the secondary market, and 36 months if stocks are newly issued by the company. Generally, a part of an employee's salary is used to purchase the shares.

Such plans are subject to shareholder approval. BlackRock generally supports the idea of employees holding company stock and given the associated retention period, we think a discount in the purchase price within 10% is reasonable.

### **Dilution**

To ensure that equity-based compensation plans operate in a way that benefits both employees and shareholders, BlackRock expects to see a limit on the amount of dilution that can occur across all plans. BlackRock may consider voting against an options plan if it may lead to over 10% cumulative dilution over ten years inclusive of existing plans, or if a plan is not transparent in demonstrating the distribution of option awards between senior executives and other staff.

# Material sustainability-related risks and opportunities

It is our view that well-managed companies will effectively evaluate and manage material sustainability-related risks and opportunities relevant to their businesses. As with all risks and opportunities in a company's business model, appropriate oversight of material sustainability considerations is a core component of having an effective governance framework, which supports durable, long-term financial value creation.

Robust disclosure is essential for investors to effectively evaluate companies' strategy and business practices related to material sustainability-related risks and opportunities. Long-term investors like our clients can benefit when companies demonstrate that they have a resilient business model through disclosures that cover governance, strategy, risk management, and metrics and targets, including industry-specific metrics. The International Sustainability Standards Board (ISSB) standards, IFRS S1 and S2,<sup>7</sup> provide companies with a useful guide to preparing this disclosure. The standards build on the Task Force on Climate-related Financial Disclosures (TCFD) framework and the standards and metrics developed by the Sustainability Accounting Standards Board (SASB), which have converged under the ISSB. We recognize that companies may phase in reporting aligned with the ISSB standards over several years. We also recognize that some companies may report using different standards, which may be required by regulation, or one of a number of voluntary standards. In such cases, we ask that companies highlight the metrics that are industry- or company-specific.

We note that climate and other sustainability-related disclosures often require companies to collect and aggregate data from various internal and external sources. We recognize that the practical realities of data collection and reporting may not line up with financial reporting cycles and companies may require additional time after their fiscal year-end to accurately collect, analyze, and report this data to investors. That said, to give investors time to assess the data, we encourage companies to produce climate and other sustainability-related disclosures sufficiently in advance of their annual meeting, to the best of their abilities.

Companies may also choose to adopt or refer to guidance on sustainable and responsible business conduct issued by supranational organizations such as the United Nations or the Organization for Economic Cooperation and Development. Further, industry initiatives on managing specific operational risks may provide useful guidance to companies on best practices and disclosures. We find it helpful to our understanding of investment risk when companies disclose any relevant global climate and other sustainability-related standards adopted, the industry initiatives in which they participate, any peer group benchmarking undertaken, and any assurance processes to help investors understand their approach to sustainable and responsible business practices. We will express any concerns through our voting where a company's actions or disclosures do not seem adequate in light of the materiality of the business risks.

## Climate and nature-related risk

While companies in various sectors and geographies may be affected differently by climate-related risks and opportunities, the low-carbon transition is an investment factor that can be material for many companies and economies around the globe.

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<sup>7</sup> The objective of [IFRS S1](#) General Requirements for Disclosure of Sustainability-related Financial Information is to require an entity to disclose information about its sustainability-related risks and opportunities that is useful to primary users of general-purpose financial reports in making decisions relating to providing resources to the entity. The objective of [IFRS S2](#) Climate-related Disclosures is to require an entity to disclose information about its climate-related risks and opportunities that is useful to primary users of general-purpose financial reports in making decisions relating to providing resources to the entity.

We seek to understand, from company disclosures and engagement, the strategies companies have in place to manage material risks to, and opportunities for, their long-term business model associated with a range of climate-related scenarios, including a scenario in which global warming is limited to well below 2°C, considering global ambitions to achieve a limit of 1.5°C. As one of many shareholders, and typically a minority one, BlackRock does not tell companies what to do. It is the role of the board and management to set and implement a company's long-term strategy to deliver long-term financial returns.

Our research shows that the low-carbon transition is a structural shift in the global economy that will be shaped by changes in government policies, technology, and consumer preferences, which may be material for many companies.<sup>8</sup> Yet the path to a low-carbon economy is deeply uncertain and uneven, with different parts of the economy moving at different speeds. BIS recognizes that it can be challenging for companies to predict the impact of climate-related risk and opportunity on their businesses and operating environments. Many companies are assessing how to navigate the low-carbon transition while delivering long-term value to investors. In this context, we encourage companies to publicly disclose, consistent with their business model and sector, how they intend to deliver long-term financial performance through the transition to a low-carbon economy. Where available, we appreciate companies publishing their transition plan.<sup>9</sup>

Consistent with the ISSB standards, we are better able to assess preparedness for the low-carbon transition when companies disclose short-, medium- and long-term targets, ideally science-based where these are available for their sector, for scope 1 and 2 greenhouse gas emissions (GHG) reductions and to demonstrate how their targets are consistent with the long-term financial interests of their investors.

While we recognize that regulators in some markets are moving to mandate certain disclosures, at this stage, we view scope 3 emissions differently from scopes 1 and 2, given methodological complexity, regulatory uncertainty, concerns about double-counting, and lack of direct control by companies. We welcome disclosures and commitments companies choose to make regarding scope 3 emissions and recognize these are provided on a good-faith basis as methodology develops. Our publicly available [commentary](#) provides more information on our approach to climate-related risks and opportunities.

In addition to climate-related risks and opportunities, the management of nature-related factors is increasingly a component of some companies' ability to generate durable, long-term financial returns for shareholders, particularly where a company's strategy is heavily reliant on the availability of natural capital, or whose supply chains are exposed to locations with nature-related risks. We look for such companies to disclose how they manage any reliance and impact on, as well as use of, natural capital, including appropriate risk oversight and relevant metrics and targets, to understand how these factors are integrated into strategy. We will evaluate these disclosures to inform our view of how a company is managing material nature-related risks and opportunities, as well as in our assessment of relevant

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<sup>8</sup> BlackRock Investment Institute, "Tracking the low-carbon transition", July 2023.

<sup>9</sup> We have observed that more companies are developing such plans, and public policy makers in a number of markets are signaling their intentions to require them. We view transition plans (TPs) as a method for a company to both internally assess and externally communicate long-term strategy, ambition, objectives, and actions to create financial value through the global transition towards a low-carbon economy. While many initiatives across jurisdictions outline a framework for TPs, there is no consensus on the key elements these plans should contain. We view useful disclosure as that which communicates a company's approach to managing financially material, business relevant risks and opportunities – including climate-related risks – to deliver long-term financial performance, thus enabling investors to make more informed decisions.

shareholder proposals. Our publicly available [commentary](#) provides more information on our approach to natural capital.<sup>10</sup>

## Key Stakeholder Interests

In order to advance long-term shareholders' interests, companies should consider the interests of the various parties on whom they depend for their success over time. It is for each company to determine their key stakeholders based on what is material to their business and long-term financial performance. For many companies, key stakeholders include employees, business partners (such as suppliers and distributors), clients and consumers, regulators, and the communities in which they operate.

As a long-term shareholder on behalf of our clients, we find it helpful when companies disclose how they have identified their key stakeholders and considered their interests in business decision-making. In addition to understanding broader stakeholder relationships, BIS finds it helpful when companies consider the needs of their workforce today, and the skills required for their future business strategy. We are also interested to understand the role of the board, which is well positioned to ensure that the approach taken is informed by and aligns with the company's strategy and purpose.

Companies should articulate how they address material adverse impacts that could arise from their business practices and affect critical relationships with their stakeholders. We encourage companies to implement, to the extent appropriate, monitoring processes (often referred to as due diligence) to identify and mitigate potential adverse impacts and grievance mechanisms to remediate any actual adverse material impacts. In our view, maintaining trust within these relationships can contribute to a company's long-term success.

## Shareholder proposals

In most markets in which BlackRock invests on behalf of clients, shareholders have the right to submit proposals to be voted on by shareholders at a company's annual or extraordinary meeting, as long as eligibility and procedural requirements are met. The matters that we see put forward by shareholders address a wide range of topics, including governance reforms, capital management, and improvements in the management or disclosure of sustainability-related risks.

BlackRock is subject to legal and regulatory requirements in the U.S. that place restrictions and limitations on how BlackRock can interact with the companies in which we invest on behalf of our clients, including our ability to submit shareholder proposals. We can vote, on behalf of clients who authorize us to do so, on proposals put forth by others.

When assessing shareholder proposals, we evaluate each proposal on its merit, with a singular focus on its implications for long-term financial value creation by that company. We believe it is helpful for companies to disclose the names of the proponent or organization that has submitted or advised on the proposal. We consider the business and economic relevance of the issue raised, as well as its materiality and the urgency with which our experience indicates it should be addressed. We would not support proposals that we believe would result in over-reaching into the basic business decisions of the company. We take into consideration the legal effect of the proposal, as shareholder proposals may be advisory or

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<sup>10</sup> Given the growing awareness of the materiality of these issues for certain businesses, enhanced reporting on a company's natural capital dependencies and impacts would aid investors' understanding. In our view, the final recommendations of the [Taskforce on Nature-related Financial Disclosures](#) may prove useful to some companies. We recognize that some companies may report using different standards, which may be required by regulation, or one of a number of other private sector standards.

legally binding depending on the jurisdiction, while others may make requests that would be deemed illegal in a given jurisdiction.

Where a proposal is focused on a material business risk that we agree needs to be addressed and the intended outcome is consistent with long-term financial value creation, we will look to the board and management to demonstrate that the company has met the intent of the request made in the shareholder proposal. Where our analysis and/or engagement indicate an opportunity for improvement in the company's approach to the issue, we may support shareholder proposals that are reasonable and not unduly prescriptive or constraining on management.

We recognize that some shareholder proposals bundle topics and/or specific requests and include supporting statements that explain the reasoning or objectives of the proponent. In voting on behalf of clients, we do not submit or edit proposals or the supporting statements – we must vote yes or no on the proposal as phrased by the proponent. Therefore, when we vote in support of a proposal, we are not necessarily endorsing every element of the proposal or the reasoning, objectives, or supporting statement of the proponent. We may support a proposal for different reasons from those put forth by the proponent, when we believe that, overall, it can advance our clients' long-term financial interests. We would normally explain to the company our rationale for supporting such proposals.

Alternatively, or in addition, we may vote against the election of one or more directors if, in our assessment, the board has not responded sufficiently or with an appropriate sense of urgency. We may also support a proposal if management is on track, but we believe that voting in favor might accelerate efforts to address a material risk.

## **Other corporate governance matters**

In our view, shareholders have a right to timely and detailed information on the financial performance and viability of the companies in which they invest. In addition, companies should publish information on the governance structures in place and the rights of shareholders to influence these. The reporting and disclosure provided by companies helps shareholders assess the effectiveness of the board's oversight of management and whether investors' economic interests have been protected. We believe shareholders should have the right to vote on key corporate governance matters, including changes to governance mechanisms, to submit proposals to the shareholders' meeting and to call special meetings of shareholders.

## **Amendments to articles of association and bylaws**

These proposals vary from routine changes such as reflection of regulatory change, to significant changes that substantially alter the governance of the company. We will review these proposals on a case-by-case basis and support those proposals that we believe are in the best interests of shareholders. We expect all listed companies to disclose a comparison table to detail proposed amendments and relevant rationales for their article of association and bylaws. If disclosure is inadequate or significant concerns are identified, BlackRock may consider voting against these proposals.

## **Anti-takeover devices**

BlackRock believes that transactions or practices that are intended to impede a potential takeover can be limiting to shareholders. BlackRock will generally not support proposals that introduce or renew anti-takeover devices.

## Bundled proposals

We believe that shareholders should have the opportunity to review substantial issues individually without having to accept bundled proposals. Where several measures are grouped together, BlackRock may reject the overall proposal if it includes those that contradict or impede the rights and economic interests of shareholders.

## Voting Choice

BlackRock offers a Voting Choice program, which provides eligible clients with more opportunities to participate in the proxy voting process where legally and operationally viable. BlackRock Voting Choice aims to make proxy voting easier and more accessible for eligible clients.

Voting Choice is currently available for eligible clients invested in certain institutional pooled funds in the U.S., UK, Ireland, and Canada that utilize equity index investment strategies, as well as eligible clients in certain institutional pooled funds in the U.S., UK, and Canada that use systematic active equity (SAE) strategies. Currently, this includes over 650 pooled investment funds, including equity index funds and SAE investment funds. In addition, institutional clients in separately managed accounts (SMAs) continue to be eligible for BlackRock Voting Choice regardless of their investment strategies.<sup>11</sup>

As a result, the shares attributed to BlackRock in company share registers may be voted differently depending on whether our clients have authorized BIS to vote on their behalf, have authorized BIS to vote in accordance with a third-party policy, or have elected to vote shares in accordance with their own policy. Agreements with our clients to allow them greater control over their voting, including which policies they have selected, will be treated confidentially consistent with our treatment of similar client agreements.

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<sup>11</sup> Read more about BlackRock Voting Choice on our website here <https://www.blackrock.com/corporate/about-us/investment-stewardship/blackrock-voting-choice>

## Want to know more?

[blackrock.com/stewardship](https://blackrock.com/stewardship) | [contactstewardship@blackrock.com](mailto:contactstewardship@blackrock.com)

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