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BlackRock Updates 2022 Proxy Voting Guidelines and Stewardship Expectations and Publishes Annual Letter to CEOs

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Larry Fink's Letter to CEOs

On January 18th, Larry Fink, the CEO of BlackRock, published his 2022 Letter to CEOs, titled "The Power of Capitalism."

The letter focuses on the following key topics while building on themes of prior years:

- **Stakeholder capitalism**, including the central role that corporate purpose plays, together with consistent values and consideration of stakeholders in determining the long-term success of companies. The value of corporate purpose is a theme Fink discussed at length in his 2018 letter.
- **Shifting workplace dynamics** and the evolving relationship between employers and employees
- **Investment in innovation**, namely the disruptive impact and opportunities presented by the global transition to a net zero carbon economy
- A focus on **stewardship and engagement**, not divestment, to drive decarbonization
- Expansion of the **proxy voting process** to institutional clients and, looking to the future, individual owners

Stakeholder Capitalism. This year, Fink's letter opens with an exposition of stakeholder capitalism. He states, "Stakeholder capitalism is not about politics. It is not a social or ideological agenda. It is not "woke." *It is capitalism*, driven by mutually beneficial relationships between you and the employees, customers, suppliers, and communities your company relies on to *prosper*. This is the power of capitalism." He continues on to emphasize that effective stakeholder capitalism is the means by which companies achieve durable long-term profitability. Furthermore, Fink opines that, in a tumultuous global environment, a company's purpose is its "north star," and that stakeholders expect to hear directly from CEOs on societal issues that are key to a company's long-term success. The letter also highlights BlackRock's launch of its Center for Stakeholder

Capitalism. On the heels of Fink's 2022 letter, we expect that purpose statements may reemerge as a topic this year.

Workplace Evolution. The letter's commentary on the employee-employer relationship discusses the disruption accelerated by the Covid-19 pandemic. In particular, it takes note of the increased focus on issues like employee pay and turnover, as well as racial equity, childcare and mental health, that an employer must prioritize to remain competitive for talent. See the Sidebar for detail on questions BlackRock poses to companies with respect to both workplace evolution and decarbonization.

Investment Opportunity Through Decarbonization. Climate change continues to be a focus in the letter. This year, the letter highlights BlackRock's expectation that companies play a role in

decarbonization of the global economy. In Fink's view, decarbonization will create "the greatest investment opportunity of our lifetime." How companies navigate the global energy transition will be a key consideration in future capital allocation decisions, both in the deployment of capital to new ventures, as well as the transition of capital from traditional to ESG-focused indexes and products. Mirroring 2022 policy updates, the letter also specifically asks companies to set short-, medium-, and long-term targets for greenhouse gas reductions.

Decarbonization Not Divestment. Importantly, the letter highlights that BlackRock is not pursuing a strategy of divestment from the oil and gas sector, and does not wish to encourage the transition of carbon-intensive assets from the public markets to sources of private financing. Consistent with these statements, BlackRock's Global Principles ask that companies disclose how their capital allocation across fossil fuels, alternatives and transition technologies aligns with their strategies and emissions reduction targets. Note that State Street CEO Cyrus Taraporevala's January 12th letter addressed the topic of divestment in a similar manner.

Expansion of the Proxy Voting Process. Finally, the letter notes the importance of stewardship to understand how companies are fulfilling their responsibilities to shareholders. Regarding proxy voting, following on from its announcement last year that enabled certain institutional clients to directly vote shares under BlackRock's management, BlackRock foreshadows further expansion in stating, "We are committed to a future where every investor – even individual investors – can have the option to participate in the proxy voting process if they choose." It is the firm's intention to expand further the participation of individual investors.

Fink's 2022 letter specifically asks companies:

Evolving Workplace Expectations

"Disclose how evolving workplace expectations are impacting a company and its industry, including: "What are you doing to deepen the bond with your employees? How are you ensuring that employees of all backgrounds feel safe enough to maximize their creativity, innovation and productivity? How are you ensuring your board has the right oversight of these critical issues? How is your company's culture adapting to this new world? How has the changing employer/employee relationship affected your industry and your company?"

Decarbonization

"What are you doing to disrupt your business? How are you preparing for and participating in the net zero transition? As your industry gets transformed by the energy transition, will you go the way of the dodo, or will you be a phoenix?"

A link to the full letter can be found here.

BlackRock Updated Voting Guidelines

In December 2021, BlackRock released its 2022 U.S. proxy voting guidelines, along with updated global principles that outline its 2022 stewardship expectations. Key changes to its U.S. proxy voting guidelines are discussed below.

Climate Risk

BlackRock's updates expand upon its expectations with respect to company and board management and oversight of climate risk. BlackRock continues to request that all companies "articulate how they are aligned to a scenario in which global warming is limited to well below 2°C, moving towards global net zero GHG emissions by 2050."

New for 2022, its Global Principles further ask that companies disclose their climate transition plans and demonstrate how those plans are resilient under the global aspiration to limit global warming to 1.5° C, and disclose how considerations related to having a reliable energy supply and just transition affect their plans.

Moreover, the revised US guidelines specifically encourage companies to set short-, medium- and long-term science-based targets, and how their capital allocation across alternatives, transition technologies and fossil fuels is consistent with such targets and a company's strategy. Lastly, as revised, BlackRock's guidelines now explicitly link disclosure alignment with TCFD as well as a company's short-, medium- and long-term Scope 1 and 2 emissions reduction targets to BlackRock's voting on director elections and shareholder proposals.

ESG Disclosure Expectations

Last year, BlackRock's guidelines articulated its expectations that companies produce disclosure aligned with the recommendations of the TCFD and the standards developed by the Sustainability Accounting Standards Board (SASB). In this year's update, BlackRock broadens its expectations, noting its expectations of "investor-relevant, industry-specific, material metrics and rigorous targets, aligned with SASB or comparable sustainability reporting standards." This change is likely due to the formation of the International Sustainability Standards Board, or ISSB, as in referencing SASB, the 2022 guidelines also acknowledge the work underway by the ISSB, expected to culminate in initial standards by mid-2022.

Additionally, BlackRock now requests that companies disclose "any supranational 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 conduct."

Board Composition and Effectiveness

BlackRock has updated its policies related to board composition and effectiveness. The updates explicitly quantify that boards should aspire to 30% diversity. In addition to continuing its previous policy of encouraging boards to have at least two female directors, BlackRock now suggests boards also have at least one director who identifies as a member of an underrepresented group. Further, BlackRock's 2022 guidelines add discussion of the perceived benefits of board diversity, in particular highlighting, "Over time, [greater diversity in the board room] can also promote greater diversity and resilience in the leadership team and workforce more broadly, enabling companies to develop businesses that more closely reflect and resonate with the customers and communities they serve."

BlackRock's updated policies have several notable changes with respect to disclosure expectations. While 2021's policies *encouraged* companies to disclose various metrics surrounding board composition, 2022's policies are now *asking* companies to do so. The updated policies now *ask* the board to disclose whether it considers a diverse slate of nominees for all available board nominations. BlackRock has removed language from 2021 that encouraged disclosure of "measurable milestones to achieve a boardroom reflective of multi-faceted racial, ethnic, and gender representation," and added a request that companies disclose "the aspects of diversity that the company believes are relevant to its business and how the diversity characteristics of the board, in aggregate, are aligned with a company's long-term strategy and business model."

In the case of new directors, BlackRock now requests "sufficient information on the individual candidates so that shareholders can assess the suitability of each individual nominee and the overall board composition."

Director Elections

BlackRock's Global Principles have been similarly updated to highlight that engagement provides the opportunity to hear directly from companies on how they believe their actions align with sustainable, long-term value creation, and that to the extent BlackRock has concerns about a company's approach, it may vote against the re-election of directors with responsibility for the issue in question. Further, it has added "financial" to the list of ESG factors it expects boards to oversee, consistent with the themes of Fink's letter summarized above.

Auditors and Audit-Related Issues

BlackRock updated its Global Principles to note that it expects assumptions pertaining to the impact of the transition to a low carbon economy on a company's business model and asset mix will be subject to increased investor scrutiny over time, given the potential ability of those assumptions to materially impact financial performance.

Corporate Form

The 2022 proxy voting guidelines include a new section detailing BlackRock's approach to corporate form, including when a company intends to convert to a public benefit corporation structure. BlackRock details specific expectations for such proposals, including clear articulation of how the interests of shareholders and different stakeholders would be augmented or adversely affected, and the accountability and voting mechanisms that would be available to shareholders.

The guidelines provide a distinction between management proposals on this topic and shareholder proposals. BlackRock will generally support management proposals if its analysis indicates that shareholders' interests are adequately protected, whereas BlackRock evaluates shareholder proposals on a case-by-case basis.

Human Capital Management

BlackRock has added language in its 2022 guidelines indicating an expectation that companies demonstrate "a robust approach" to human capital management (HCM) and provide sufficient disclosure to enable shareholders to understand how a company's HCM approach aligns with its strategy and business model. Although this update refined BlackRock's expectations for the company board role relative to HCM, we do not believe this revision is intended to de-emphasize the importance of board oversight over such matters.

Executive Compensation

For 2022, BlackRock has refined its guidelines regarding incentive compensation. The 2022 guidelines indicate that BlackRock will support incentive plans that foster the sustainable achievement of results – ***both financial and nonfinancial***, ***including ESG*** – consistent with the company's strategic initiatives. The references to nonfinancial results and the specific callout of ESG are new for 2022. Furthermore, BlackRock’s Global Principles provide that, when a company incorporates ESG metrics into its executive compensation plans, the metrics used should be “as rigorous as other financial or operational targets.”

With respect to say on pay proposals, companies should take note that BlackRock has removed language from its guidelines that previously provide it would consider voting against compensation committee members in instances where it votes against a company’s say on pay proposal. As revised, it appears BlackRock’s policy is to vote against relevant compensation committee members in all instances where it votes against a say on pay proposal due to a perceived failure to align pay with performance. BlackRock's guidelines also strengthen language regarding annual frequency with respect to say on pay votes. Historically, BlackRock deferred to the board's judgment on appropriate frequency. For 2022, BlackRock’s policies provide that shareholders should have the ability to vote on such matters on an annual basis.

BlackRock has also added equity compensation plan concerns to its list of matters that may cause it to vote against responsible directors. Specifically, it may now vote against members of a company’s audit committee where it does not view a company’s proposed equity compensation plan as being aligned with shareholder interests.

Corporate Political Activities

On the subject of corporate political activities, BlackRock has narrowed the scope of its guidelines. The policy now provides that BlackRock will: “evaluate whether there is general consistency between a company’s stated positions on policy matters material to its strategy and the material positions taken by significant industry groups of which it is a member.” The language surrounding *material positions taken by significant industry groups* is an update from 2021, which did not include reference to ***material*** positions or ***significant*** industry groups.

Additionally, BlackRock expands upon its 2021 language regarding voting on shareholder proposals. The previous guidelines noted that BlackRock may support shareholder proposals seeking additional disclosure in instances where it identifies misalignment. In the updated guidelines, BlackRock includes language that indicates potential support of proposals if further transparency may clarify how the company’s political activities support its long-term strategy.

Shareholder Proposals

BlackRock has updated its Global Principles to add new language noting that it may support shareholder proposals “if we believe management is on track, but we believe that voting in favor might accelerate progress." This update is consistent with certain rationales BlackRock provided in its voting bulletins for 2021 annual meetings, and will be important for companies to keep in mind as they assess the likelihood of support for anticipated proposals at upcoming annual meetings.

If you have questions or comments, please email info@georgeson.com or call 212 440 9800.