BLACKROCK

13 December 2013

**Catherine Woods**
**Financial Reporting Council**
Fifth Floor
Aldwych House
71-91 Aldwych
London WC2B 4HN

Submitted via email to: remcon@frc.org.uk

**RE: FRC – Directors' Remuneration Consultation Document**

Dear Catherine,

BlackRock is pleased to have the opportunity to respond to the Financial reporting Council's (FRC) consultation on directors' remuneration.

BlackRock is one of the world's pre-eminent investment management firms and a premier provider of global investment management, risk management and advisory services to institutional and retail clients around the world.

As of 30 September 2013, the assets BlackRock manages on behalf of its clients £2.54 trillion across equity, fixed income, cash management, alternative investment and multi-investment and advisory strategies including the iShares® exchange traded funds. Through BlackRock Solutions®, the firm also offers risk management, strategic advisory and enterprise investment system services to a broad base of clients, including governments and multi-lateral agencies.

BlackRock has a pan-European client base serviced from 22 offices across the continent. Public sector and multi-employer pension plans, insurance companies, third-party distributors and mutual funds, endowments, foundations, charities, corporations, official institutions, banks and individuals invest with BlackRock.

We welcome the opportunity to address, and comment on, the issues raised by this consultation and we will continue to work with the FRC on any specific issues that may assist in improving the UK Corporate Governance Code.

## Key points

### Extended Clawback provisions

BlackRock supports the flexible approach taken by the Code allowing companies to adopt the most suitable incentive structure to facilitate the execution of strategy, and therefore considers that the current wording of the Code to be sufficient in stating that "consideration should be given to the use of provisions that permit the company to reclaim variable components in exceptional circumstances of misstatement or misconduct".

We do not believe that the Code needs to specify the circumstances under which payments could be recovered and/or withheld as it is the role of the Board of the Company to determine those situations which might lead to applying 'clawback' provisions or 'malus' provisions.

It is important to distinguish between clawback provisions or malus provisions. The former is defined as recovery of sums paid and deals with situations involving criminal activity or fraud. The latter refers to a withholding of sums to be paid.

### Remuneration Committee Membership

We believe that the Chairman of the Board is best placed to evaluate the composition of the Board and the Remuneration Committee. From our perspective as a shareholder, a director's expertise, relevant business and industry experience and ability to contribute to the work of the Board are the key considerations in his or her appointment to the Board and/or Remuneration Committee.

### Votes Against the Remuneration Report

BlackRock supports the FRC Stewardship Code and its principle of on-going engagement between companies and their shareholders. We firmly believe that the objective of such engagements should be thoughtful decisions that lead to enhanced long-term value. Hasty solutions taken to meet a reporting deadline and not necessarily based on a sound understanding of shareholder concerns may not meet such an objective.

We are supportive of the feedback mechanism outlined by the Regulations, and do not regard it to be necessary to change the Code to provide additional reporting deadlines.

### Other Possible Changes

We are supportive the UK Corporate Governance Code in its current form and believe it should continue to be reviewed on a regular basis to ensure it reflects current best practices.

## Responses

**Extended Clawback Provisions**

1. ***Is the current Code requirement sufficient, or should the Code include a "comply or explain" presumption that companies have provisions to recover and/or withhold variable pay?***

We consider the current wording of the Code which requires companies to consider "the use of provisions that permit the company to reclaim variable components in exceptional circumstances of misstatement or misconduct" to be sufficient. Boards and Remuneration Committees should be afforded the flexibility to design the incentive structure which they believe best facilitates the execution of strategy. Similarly, they should be afforded the flexibility to put in place the proper risk mitigation tools, taking into consideration the company's own industry, risk profile and business cycle. Clawback could be one such mechanism. While we are supportive of the concept of clawback, we believe consideration should be given to its practical implications as well as how such mechanisms operate in practice.

Should the Code be revised to include a "comply or explain" provision to require all public companies to adopt clawback, it would be necessary to determine whether the Code should also provide guidance on whether the mechanism should cover all variable pay, or that only certain structures (annual incentive, deferred shares, share incentives, etc.) should be within scope.

2. ***Should the Code adopt the terminology used in the Regulations and refer to "recovery of sums paid" and "withholding of sums to be paid"?***

We support regulatory coherence and therefore believe that the Code should be aligned with the new Regulations to minimise confusion. In this regard, it would be preferable to amend the Code such that it refers to the "recovery of sums paid" and the "withholding of the payment of any sum".

3. ***Should the Code specify the circumstances under which payments could be recovered and/or withheld? If so, what should these be?***

We believe the Code should continue to provide guidance on its provisions, although it might prove challenging to outline circumstances under which payments could be recovered and/or withheld. One of the challenges in setting policies on remuneration and related areas is that it is difficult to foresee every potential situation in which clawback could apply. There is a risk that any list of such circumstances outlined by the Code could be taken as exhaustive and thus provide sufficient foundation for a director to seek legal recourse should a company seek to apply clawback in a previously undefined situation. We believe the Board of Directors, as the governing body elected by shareholders, is best placed to determine which payments should be recovered and/or withheld and when.

4. ***Are there practical and/or legal considerations that would restrict the ability of companies to apply clawback arrangements in some circumstances?***

We believe there are practical and legal considerations that could restrict the ability of companies to apply clawback arrangements, which is a recovery of sums paid. For example, in any complex situation involving possible wrongdoing, it may take a long time (years in some instances) to get a resolution of fact-finding, in which case any requirement to apply a clawback provision in advance of such fact-finding resolution could subject the company to legal challenge.

While we consider 'malus', or performance adjustment, which is a withholding of sums to be paid, to be subject to fewer complexities, we recognise that there are some concerns around malus, similar to the example explained above.

If a company plans to introduce a provision to reclaim variable components of pay, there should be absolute clarity as to whether the company is instituting a clawback provision or a malus provision, or both and how it intends to deal with the challenges explained above.

**Remuneration committee membership**

***5. Are changes to the Code required to deter the appointment of executive directors to the remuneration committees of other listed companies?***

We regard the current Code's provisions on Board and Sub-Committee structure and balance as sufficient. In this regard, that remuneration committees comprise three or, in the case of smaller companies, two, independent non-executive directors, is adequate guidance.

We believe that the Chairman of the Board is best placed to evaluate its composition, including that of the sub-committees. From our shareholder perspective, expertise, relevant business and industry experience and an ability to contribute to the work of the Board are the key considerations in appointing a member to the Board and/or Remuneration Committee. We believe that executive directors can bring valuable industry, executive and board-level experience to the Boards of other listed companies where they serve as non-executives. With regards to Remuneration Committees specifically, executive directors can bring knowledge both on the practical effect of various incentive designs as well as on what truly motivates an executive director.

Further, such an amendment to the Code would require guidance on whether the restriction should be extended to include any director who has previously served in an executive capacity. There are several unintended consequences in deterring the appointment of executive directors, past or present, to serve on Remuneration Committees. The pool of Remuneration Committee candidates would shrink. In addition, Board sizes could become unwieldy as token directors could be appointed to the Remuneration Committee, and former or serving executives to the main Board for the benefit of their experience or networks.

We believe that directors should themselves ensure they are not conflicted when taking up the role, but only in respect of their foreseen duties at that particular company.

**Votes against the remuneration resolutions**

***6. Is an explicit requirement in the Code to report to the market in circumstances where a company fails to obtain at least a substantial majority in support of a resolution on remuneration needed in addition to what is already set out in the Regulations, the guidance and the Code?***

***If yes, should the Code:***

- ***a. set criteria for determining what constitutes a 'significant percentage';***
- ***b. specify a time period within which companies should report on discussions with shareholders;***
- **c.** ***specify the means by which companies should report to the market and, if so, by what method*****?**

BlackRock supports the FRC Stewardship Code and its principle of on-going engagement between companies and their shareholders. We firmly believe that the objective of such engagements should be thoughtful decisions that lead to enhanced long-term value. Hasty solutions taken to meet a reporting deadline and not necessarily based on a sound understanding of shareholder concerns may not meet such an objective.

Although we are supportive of the feedback mechanism outlined by the Regulations, we do not regard as necessary to change the Code to provide additional reporting deadlines.

We note that greater clarity on what constitutes a "significant" percentage would have helped give a more precise answer to this question. We believe that this percentage would vary from company to company, not least as a reflection of its shareholder register and any concentration

of ownership. There are listed companies, which are widely held and have a dispersed shareholder base. Equally, there are listed companies, which have a large or controlling shareholder. If it is deemed necessary to define what percentage is to be considered "significant", then we believe the FRC should work with companies to help define this percentage.

We do not consider additional reporting prior to the publication of the Remuneration Report in the next Annual Report to be required where a company does not obtain at least a substantial majority support of a resolution on remuneration. We believe that the company should be given the flexibility to address shareholder concerns in a considered and constructive manner, which allows for the thoughtful analysis of the feedback by the Remuneration Committee. The Regulations required companies to report on discussions with shareholders in the following year's Annual Report. Amending the Code to require reporting in a shorter timeframe risks hampering the integrity of the process as discussions with shareholders could take longer than the time provided by this window. It is important to have a flexible timeframe to permit a thorough review of shareholder concerns over the proposed policy or implementation votes. Further, such a reporting deadline could lead to boilerplate statements, which do little to improve the quality of engagement and the output of the consultation process.

Similarly, we believe that the company should be able to determine its desired form of reporting, if it is making a statement in addition to what it publishes in its Annual Report.

***7. Are there any practical difficulties for companies in identifying and/or engaging with shareholders that voted against the remuneration resolution/s?***

Yes. From an operational perspective, the voting chain is rather complex. It could be challenging for a company to know exactly who its shareholders are, let alone which shareholders would have been the ones to withhold support. There could be some difficulty in reaching smaller or retail shareholders before the next general meeting, as the beneficial ownership details may not be transparent to the company. The European Commission, as part of its Corporate Governance Action Plan, intends to undertake an initiative to improve the visibility of shareholdings in the European Union as part of its legislation on securities law. We welcome this pan-European regulatory solution. In addition to these operational complexities, some shareholders may not be willing to engage. However, companies with good corporate governance practices will have already been engaging with their shareholders on a regular and consistent basis, including having meaningful dialogue including on remuneration. Therefore, if the shareholders are holding up the principles of the FRC Stewardship Code, companies should already know which of their larger shareholders would have withheld support.

**Other Possible Changes**

***8. Is the Code compatible with the Regulations? Are there any overlapping provisions in the Code that are now redundant and could be removed?***

We are supportive the UK Corporate Governance Code in its current form and believe it should be reviewed on a regular basis to ensure it reflects current best practices.

***9. Should the Code continue to address these three broad areas? If so, do any of them need to be revised in the light of developments in market practice?***

The Code is sufficient in covering the three highlighted broad areas.

## Conclusion

We appreciate the opportunity to address and comment on the issues raised by the Consultation Document and will continue to work with the FRC on any specific issues which may assist in improve the UK Corporate Governance Code.

We would welcome any further discussion on any of the points that we have raised.

Yours faithfully,

**Amra Balic**
Director
Head of Corporate Governance
& Responsible Investment EMEA
+44 (0)20 7743 5281
amra.balic@blackrock.com
12 Throgmorton Avenue
London EC2N 2DL

**Jennifer Law**
Associate
Corporate Governance
& Responsible Investment EMEA
+44 (0)20 7743 2181
jennifer.law@blackrock.com
12 Throgmorton Avenue
London EC2N 2DL