BlackRock

Corporate governance and proxy voting guidelines for New Zealand securities

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These guidelines should be read in conjunction with BlackRock's Global Corporate Governance and Engagement Principles – 2011.

Introduction

Our policy for New Zealand is based on the guidelines established by the Securities Commission of New Zealand - Corporate Governance in New Zealand Principles and Guidelines and the Corporate Governance Best Practice Code of the New Zealand Stock Exchange (NZSX).

Our approach to voting and corporate engagement is informed by the Financial Services Council Guidance Note No.20 "Corporate Governance: A Guide for Fund managers and Corporations" and other 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 active members of each of these organisations and thus believe that their guidance is consistent with our own principles.

We expect every NZSX listed company to provide a meaningful statement as how the corporate governance principles it follows materially differ from the Corporate Governance Best Practice Code as set out in the Appendix to the NZSX Listing Rules.

Engagement

BlackRock takes an integrated approach to corporate governance and engagement, to the extent possible, as we believe this approach results in both better informed decisions and a more consistent dialogue with companies. Activities are coordinated by the Australian and New Zealand Corporate Governance and Responsible Investment (CGRI) team.

We have meetings and discussions with non-executive directors to discuss aspects of corporate governance such as management of succession planning of the board, executive remuneration, board structure and performance and any environmental and social issues which we believe have the potential to unnecessarily increase the risk profile of the company.

Proxy Voting Approach

BlackRock is one of the world's largest institutional investors, with extensive experience globally. The universe we cover in New Zealand includes but is not limited to the NZSX 50. BlackRock aims to vote at 100% of the annual and extraordinary shareholder meetings where we have the voting authority to do so.

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. Where we decide to vote against management or abstain from voting on a particular proposal we advise the company in advance whenever possible.

Corporate Governance and Proxy Voting Guidelines

These guidelines are divided into seven key themes as follows:

- Boards and directors;
- Auditors and audit-related issues;
- Risk Management;
- Capital structure, mergers, asset sales and other special transactions;
- Remuneration and benefits;
- Social, ethical and environmental issues;
- General corporate governance matters.

Boards and Directors

Composition of the board of directors

The board of a listed company should comprise competent individuals who have the requisite skills and experience to fully discharge their duties to shareholders. BlackRock expects the independent directors to possess between them the necessary breadth of experience and diversity of skills to enable them to discharge their duties to shareholders.

Assessment of independence

An independent director is a non-executive director non-executive director and generally should:

- Have no familial or material business or financial or perceived relationship with the company, its executives or other board members (except for board service and annual fees paid for that service) which may interfere with the NED's ability to act in the best interests of the company;
- Have not been an employee of the company within the last three years, Further, a non-executive director who has been an employee of the company as a senior executive is not considered to be independent unless there has been a break of at least three years between leaving employment becoming a non-executive director of the company;
- Have not been within the last three years a principal or employee of a professional advisor to the company or a related company;
- Not participate in any equity based remuneration that involves vesting based on performance of the company or continuing service as a non-executive director;
- Not control more than 5% or more of the company's voting securities or is an executive or other representative of a company that owns or controls more than 5% or more of the company's voting securities. Where a non-executive director was a representative of such a former substantial security but remains on the board after the former substantial security holder disposes of the holding, and in the absence of any other relationship between the company and the non-executive director or the former substantial security holder, we will consider reclassifying the non-executive director as independent;
- Be classified by the company as independent;
- Not hold cross-directorships or significant links with other directors through the involvement in other companies or bodies;
- Have not received fees or income for services to the company, except for board service and annual fees paid for that service, and which are significant in relation to the non-executive director fees received by the director;
- Not be a partner/director or senior executive of a professional services firm such as an accounting firm, consulting firm, law firm or investment bank where the firm is paid for services and not the individual directly;
- Not be a material supplier or customer of the company or another group member or an officer of or otherwise associated directly or indirectly with a material supplier or customer:

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- Have no material contractual relationship with the company or another group member other than as a director of the company;
- Be free from any interest and any business or other relationship which could, or could reasonably be perceived to, materially interfere with the director's ability to act in the best interests of the company.

Appointment/Reappointment Procedure

The company should have a formal and transparent procedure for the appointment and re-appointment of directors. The board should disclose in the annual report the required mix of skills, experience and other qualities, including core competencies that each director brings to the board, the process by which candidates are identified and selected including whether professional search firms have been engaged to identify and/or assess candidates, the procedures used to ensure a diverse range of candidates is considered and factors taken into account in the selection process. The annual corporate governance statement should also disclose the process adopted by the board to evaluate the performance of each director. BlackRock believes that annual performance reviews of the non-executive directors, including the chairman contribute to a more efficiently functioning board.

Diversity

BlackRock supports the proposal of the ASX Corporate Governance Council to require companies on an "if not, why not" basis to adopt and disclose a diversity policy that includes measurable objectives relating to gender.

Independent chairman

BlackRock expects the chairman to be independent. Where the chairman is not considered to be independent BlackRock expects a cogent explanation to be provided by the company and the independent directors to appoint one of their own as the lead independent director. We believe that the responsibilities of the lead independent director should include but are not limited to:

- Preside at all meetings of the board at which the chairman is not present, including sessions of the independent directors;
- Be authorized to call meetings of the independent directors;
- Serve as principal liaison on board-wide issues between the independent directors and the chairman;
- Approve the quality, quantity, appropriateness and timeliness of information sent to the board as well as approving meeting agenda items;
- Facilitate the board's approval of the number and frequency of board meetings, as well as meeting schedules to assure that there is sufficient time for discussion of all agenda items;
- Be authorized to retain outside advisors and consultants who report directly to the board of directors on board-wide issues;

- Ensure that he/she be available, if requested by shareholders, when appropriate, for consultation and direct communication;
- He/she should agree to and document the split roles between a non-independent chairman, the CEO and the lead independent director and have this published on the company's website so that shareholders can understand the break out of responsibilities.

Where a company does not have an independent chairman, a lead independent director has not been appointed and a cogent explanation has not been provided, BlackRock may consider voting against the re-election of the chairman particularly if other significant corporate governance issues exist.

BlackRock may, however, vote in favour of a non-independent chairman, for example where the:

- The company is controlled and the chairman is associated with the majority shareholder; or
- The chairman is the founder or related to the founder of the company and in BlackRock's view is of crucial importance to the company and generally has substantial wealth invested in the company.

Majority of independent directors

BlackRock expects the board of a listed company to have a majority of independent directors unless an explanation is provided. Where a board does not comprise a majority of independent directors it should take particular care with its explanation for not achieving a majority given the importance to shareholders of having an effective and objective board.

In cases where the board does not comprise a majority of independent directors, BlackRock may consider voting against the re-election of a non-independent director, and/or the chair of the nomination committee, particularly if there are other corporate governance concerns regarding the company.

Number of permissible directorships an individual may hold

Non-executive directors must be able to commit an appropriate amount of time to board and committee matters. Given the nature of the non-executive role it is important that a non-executive director have spare capacity in the event of a major transaction such as a hostile takeover taking place. It is in situations like this where the demands on non-executive directors increase significantly therefore they must have the required time available to fulfill their duties to shareholders. In BlackRock's view it is the responsibility of the chairman to ensure that all the directors are able, and are participating actively and contributing to the workload of the board through formal evaluation as well as on a continuing basis.

BlackRock may vote against the re-election of a director where there is a risk the directors may be over committed in respect of membership of other boards.

NEDs who are full- time executives of other major listed companies

BlackRock has concerns when a full-time CEO accepts a non-executive role at an unrelated company. Full time CEO's are expected to work for their board and shareholders on a 24/7 basis. As discussed above non-executive directors need to have spare capacity when a major transaction occurs. BlackRock is concerned that where a full-time CEO has a non-executive director role there is a risk that the time spent in either role could be compromised. BlackRock may consider voting against a non-executive director who is also a full time CEO of a major listed company.

Length of service

BlackRock believes that shareholders are best served when there is orderly renewal of the board as this should result in directors with accumulated experience while at the same time introducing fresh minds and experience to the board. An effective renewal process will ensure that non-executive directors do not serve for such length of time that their independence may be impaired.

BlackRock will review the status of independent directors where they have been on the board in excess of 15 years. We will consider voting against the re-election of a non-executive director who has served for a period in excess of 15 years particularly if there are other concerns regarding the corporate governance of the company.

Meetings

Directors should ensure that they attend all board and committee meetings. BlackRock will consider voting against a director who fails to attend fewer than 75% of board and committee meetings in a given year, 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.

Conflicts of interest

BlackRock believes that all non-executive directors should be free from material conflicts of interest. Non-executive directors, their immediate family or related professional company, which provides material professional services to a company at any time during the last three years, may be placed in a position where they may have to make decisions that may place their interests against those of the shareholders they represent. BlackRock may vote against the re-election of a director where an identified conflict of interest may pose a significant and unnecessary risk to shareholders.

Board size

While BlackRock believes the board is best placed to determine the size of the board, we expect board size to reflect the size and complexity of the company. We do however believe that a minimum board size of five is necessary for an NZSX 20 company to ensure a good mix of skills and diversity amongst the independent directors.

External/nominated board candidates

In general BlackRock supports the recommendations of the board regarding the election of directors. BlackRock does not ordinarily support individuals who have nominated themselves for the board unless they have the support of the board. In particular, BlackRock would not support an external candidate who has a restricted agenda as directors are there to act on behalf of all shareholders and to deal with all issues that may arise. However, where we believe the addition of an external candidate to the board will add value to the skill set of the board and is in the best interests of shareholders, we will support them.

Share ownership by non-executive directors

BlackRock believes listed companies should have a clear and disclosed policy on non-executive director share ownership. We believe that non-executive directors should have some “skin in the game” in order to align their interests with those of public shareholders. Such policies should require non-executive directors, within a reasonable amount of time after joining the board, to accumulate a meaningful investment.

Where a non-executive director continues serving on a board and fails to accumulate a meaningful investment and other significant corporate governance issues exist, BlackRock may consider voting against the individual.

Disclosure of equity subject to margin calls

Directors and senior executives should be able to manage their assets in the same way that other shareholders can. Margin calls can have a significant impact on a company’s share price when the call is made on a significant shareholder.

Where a director’s investment, which is subject to margin calls, exceeds 2% of issued capital, the number of shares subject to margin calls and the margin call prices should be disclosed.

Where a company fails to disclose a material holding of a director which has been subject to margin calls and margin calls are subsequently made, resulting in a negative impact on the share price, BlackRock will consider voting against the director concerned and/or the chairman for failing to disclose such material shareholder information.

Boards and block shareholders

BlackRock acknowledges that the New Zealand market is unique by the fact that a considerable number of companies within the NZSX 50 have block shareholders. The nature of the block shareholders varies and includes family companies, large offshore listed companies, the New Zealand government and local authorities.

BlackRock does not see the presence of a block shareholder as a means to avoid addressing the issues raised above. We expect board representation of block shareholders to be equal to or less than the percentage of their shareholding. While we accept in situations where the block shareholding exceeds 50% there may not be a majority of independent directors, we do expect an independent lead director and competent independent directors to ensure protection of the minority shareholders.

Committees

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

NZSX Listing Rules requires all companies to establish an audit committee. For companies within the NZSX 20, at a minimum BlackRock expects the establishment of separate committees to focus on the issues of nomination and remuneration. For companies outside the NZSX 20, it is acceptable to have the roles of nomination and remuneration combined within the one committee.

All committees should have written terms of reference which should, inter alia, clearly set out the committee's role 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 on the company's website.

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.

For NZSX 20 we expect each committee to have at least three members. For companies outside the NZSX 20, depending on the size and complexity of the company a committee of two may be appropriate.

Audit Committee

The audit committee should comprise solely independent directors, with the appropriate mix of skills, including financial skills and experience for its role.

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.

Where the audit committee is not comprised solely of independent directors, Blackrock will consider voting against the re-election of the chairman of the audit committee or the non-independent member of the audit committee particularly if there are other corporate governance issues.

A demonstrably independent audit is essential for investor confidence. Where non-audit fees exceed the level of audit fees in any year, BlackRock will review the nature of the non-audit fees and any explanation provided by the company for the significant level of non-audit fees. Full details of all non-audit work should be disclosed. If there is a lack of explanation of the non-audit services or we believe there is a risk that the type of non-audit services provided may impair the independence of the audit, we will consider voting against the re-election of the chair of the audit committee if he/she is seeking re-election.

Other circumstances where BlackRock may consider voting against the re-election of the chair of the audit committee include but are not limited to:

- If within the last three years accounting fraud has occurred in the company;
- If within the last three years the financial statements had to be restated due to negligence or fraud;
- If the company repeatedly fails to file its financial reports in a timely fashion.

Nomination Committee

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;
- To review, at least annually of the board succession plans;
- To ensure the size and composition of the board is conducive to making appropriate decisions;
- To review the time required by a non-executive director and whether non-executive directors are meeting that requirement;
- To ensure a process for the evaluation of the performance of the board, its committees and directors and report the process to shareholders in the annual corporate governance statement;
- The appointment and re-election of directors;
- Maintaining a watching brief on the development of management and possible potential for senior executive succession planning from the level below senior executive.

BlackRock expects the board to have a formal and transparent process for the selection, appointment and re-appointment of directors to the board and disclosure of the process helps promote BlackRock’s understanding of and confidence in that process. The process should be disclosed in the annual corporate governance statement.

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 significant conflict of interest that poses a risk to shareholders;

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- If the committee fails to hold a meeting in the reporting year.

BlackRock accepts that due to the size and nature of some New Zealand companies the role of a nomination committee is undertaken by the whole board. In such circumstances BlackRock expects disclosure of why a nomination committee has not been established and how the board manages the responsibilities normally undertaken by a nomination committee.

Remuneration Committee

The remuneration committee for an NZSX 20 company should comprise solely non-executive directors. In BlackRock's view NZSX 20 companies should not have executives as members as there is the potential for, or perception of, conflict of interest of executive director involvement in board decisions on their remuneration packages.

For companies outside the NZSX 20 index, while our preference is for the remuneration committee to comprise solely non-executive directors, we understand that due to the size of the company and the development phase it may be in, the presence of the CEO on the committee may be acceptable. In such cases we expect disclosure of the protocols in place to ensure the CEO is not involved in determining his/her remuneration arrangements.

The responsibilities of the remuneration committee should include a review of and recommendations to the board on issues including but not limited to:

- The company's remuneration, recruitment, retention and termination policies and procedures for senior executives;
- Executive director and senior executive fixed and performance based remuneration to ensure that executives are motivated to pursue the long-term growth and success of the company;
- Superannuation arrangements;
- The remuneration framework for non-executive directors;
- Consult directly, ie not through the use of consultants or management, with institutional shareholders regarding their expectations.

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

- If the composition of the remuneration committee fails to meet these guidelines;
- If BlackRock has continuing concerns regarding the structure of remuneration and has raised these concerns with the company and the company continues these egregious practices;
- If the committee fails to hold a meeting in the reporting year.

Accounts, auditors and audit-related issues

Accounts

New Zealand listed companies are not required to put their annual accounts and reports to shareholders for a vote. However, some companies choose to submit their annual accounts and reports for a shareholder vote. In such cases and where there is an unqualified auditors' report, BlackRock will support such proposals.

Change of audit firm

While BlackRock accepts that it is not a requirement for companies to seek shareholder approval for the appointment of a new audit firm, we nonetheless believe that companies should put the appointment of a new audit firm to shareholders for ratification.

Authorize Board to set Auditor's Fees

For NZSX companies it is usual for the board to put a resolution to the annual general meeting seeking shareholder approval to permit the board to set the audit fees. Such proposals are not controversial and will generally be supported by BlackRock unless we have concerns regarding the overall quality of the audit firm.

Risk Management

BlackRock believes that a sound framework of risk oversight, management and control is fundamental to the long term sustainable growth of shareholder value. We expect companies to disclose to indentify their key risks and disclose how these risks are managed.

Risk management should be designed to;

- Identify, assess, monitor and manage material business risk;
- Identify material changes to the company's risk profile.

Companies should establish policies for the oversight and management of material business risks and disclose a summary of those policies.

Risk management policies should reflect the company's risk profile and should clearly describe all elements of the risk management and internal control system and any internal audit function.

The risk management policies should clearly describe the roles and accountabilities of the board, audit committee, or other appropriate board committee, management and any internal audit function.

The board should disclose whether it has received assurance from the chief executive officer (or equivalent) and the chief financial officer (or equivalent) that the declaration provided in accordance with section 295A of the Corporations is founded on a sound system of risk management and internal control and the system is operating effectively in all material respects in relation to financial reporting risks.

Capital structure, mergers, asset sales, and other special transactions

Approvals and ratification of placements

NZSX Listing Rule 7 generally limits listed companies from issuing more than 20% of equity on a non-pro rata basis in a 12 month period without shareholder approval. Companies can seek shareholder approval to exceed the 20% limit. BlackRock will consider each request to issue more than 20% of equity in a 12 month period on a case by case basis. When requesting shareholder approval to issue more than 20% of equity on a non-pro rata basis companies should disclose:

- To whom it is proposed to issue the equity;
- Details of any discounts to be offered and the rationale behind any proposed discount;
- The basis of determining the issue price;
- How the funds raised will be used:
- Alternatives considered by the company;
- Impact, if any on change of control;
- Conversion rates on equity (if applicable).

Where the above information is not forthcoming and/or the approval may result in unnecessary dilution for a majority of shareholders, BlackRock will consider voting against the approval request.

Companies can also request the ratification of previous share placements in order for that placement not to count towards their 20% allocation. If on behalf of any funds BlackRock has participated in a placement that is subject to ratification by shareholders, then pursuant to NZSX Listing Rule 7 it is unable to vote on the proposal on behalf of those funds. BlackRock will register an abstention behalf of any funds who participated in the particular placement.

Where BlackRock has not participated on behalf of any funds in a placement which shareholders are being asked to ratify for the purposes of Listing Rule 7, we expect the following information to be disclosed:

- To whom the equity was issued;
- Details of any discounts to be offered and the rationale behind any proposed discount;
- The basis of determining the issue price;
- How the funds raised will be used:
- Alternatives considered by the company;
- Impact, if any on change of control;

- Conversion rates on equity (if applicable).

Where the above information is not forthcoming, BlackRock will consider voting against the ratification request.

Mergers, asset sales, and other special transactions

In reviewing merger and asset sale proposals, BlackRock's primary concern is the best long-term economic interests of shareholders. While these proposals vary widely in scope and substance, we closely examine certain salient features in our analyses. The varied nature of these proposals ensures that the following list will be incomplete. However, the key factors that we typically evaluate in considering these proposals include:

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 a share price from 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 should be a favourable business reason for the combination.

Unanimous board approval and arm's-length negotiations are preferred. We will consider whether the transaction involves a dissenting board or does not appear to be the result of an arm's-length bidding process. We may also consider whether executive and/or board members' financial interests in a given transaction appear likely to affect their ability to place shareholders' interests before their own.

Remuneration and benefits

Introduction

The key purpose of remuneration 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. Each company faces different issues at different times, has different value drivers and accordingly, BlackRock believes that each company should structure their remuneration policies and practices in a manner that suits the needs of that particular company.

When assessing remuneration policies and practices of NZSX listed companies BlackRock is looking for a cogent explanation for the policies used and in respect of executive remuneration in particular, a clear link to the board's stated strategy.

Companies listed on both NZSX and ASX

BlackRock expects companies listed on both the NZSX and ASX, while legally not entitled obliged, to submit a remuneration report for shareholder vote as required by section 300AA of the Australian Corporations Act.

Non-executive director remuneration

The role of the non-executive director is to monitor the strategy, performance and remuneration of the executives and to protect the interests of shareholders in the long term. Non-executive directors should receive sufficient remuneration to attract and retain suitably qualified non-executive directors and encourage them to undertake their role diligently.

The executive arm and any major shareholder should not have any undue influence over the remuneration of non-executive directors.

Structure on non-executive director remuneration

Non-executive director remuneration 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 non-executive director remuneration 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.

Non-executive directors should receive a fixed annual fee, including additional fixed fees for board committee membership for their services. BlackRock supports non-executive directors entering into "salary sacrifice" arrangements whereby a portion of their fees is received by way of fully paid shares purchased on market. Such arrangements assist in aligning the interests of non-executive directors with those of shareholders.

Cap on fees paid to non-executive directors

It is a requirement under NZSX Listing Rules that listed companies obtain shareholder approval for any increase in the in the cap on non-executive fees, or alternatively, the individual remuneration paid to non-executive directors.

BlackRock considers requests for an increase in the fee cap on a case by case basis. We expect the explanatory notes to the meeting to clearly explain why the increase is being sought, the proposed level of non-executive director fees, including additional amounts for service on committees and any proposed changes to the size of the board to be disclosed.

Option Grants and performance based remuneration to non-executive directors

BlackRock does not generally support the granting of options to non-executive 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 of the shareholders they represent.

Non-executive directors should not receive performance based remuneration as to do so would more closely align their interests with those of management, whose performance and remuneration they are intended to monitor on behalf of shareholders.

Where options or performance based remuneration has been granted to non-executive directors, BlackRock will consider voting against any such proposals and the re-election of the chair of the remuneration committee who must take responsibility for such poor remuneration structures.

For smaller companies in a development/exploration phase such as biotech or mining companies, which typically have high cash burn rates and little or no income from operations, BlackRock will support the grant of options or share rights to non-executive directors where the options are issued in lieu of cash fees (as a cash saving measure), there are no performance conditions and full vesting occurs within 12 months of grant date.

Retirement benefits

Non-executive directors should not receive any form of service contingent retirement benefit. Such remuneration merely rewards a non-executive director for long service and may inhibit a non-executive director from resigning from the board if an issue of conflict or any other issue that would impair a director's independence arises.

Hedging of securities

Given the nature of the role of the non-executive director and his/her access to information, in BlackRock's view it is inappropriate for non-executive directors to enter into hedging arrangements relating to their direct and indirect shareholdings.

As discussed above, in certain circumstances BlackRock believes directors should disclose shares subject to margin calls.

Executive Remuneration

Given the uniqueness of each New Zealand listed company, and the numerous industries represented on the NZSX, we do not believe there is a "one size fits all" in respect of the structure of executive remuneration. However, there are aspects of executive remuneration that are considered to be part of an evolving framework that we typically see. Where there is a significant departure from this framework, a cogent explanation is required and will be taken into account by BlackRock when assessing executive remuneration issues.

Executive remuneration contracts

Disclosure to the NZSX

Upon appointment of an executive director or where there have been material changes to the terms of an executive director's contract of employment, BlackRock expects disclosure of the key features of contracts to the NZSX. Such disclosure should include, but is not limited to the following features of the contract of employment:

- Period of the contract;
- Quantum of fixed remuneration;
- Structure of any performance based remuneration;
- Notice period and termination provisions;
- Sign-on remuneration;
- Retention provisions;
- Change on control provision and the impact on variable remuneration;
- Any other material issues which will assist shareholders to fully understand the terms.

Length of contracts

While it is reasonable for a contract to have an initial term of up to three years, BlackRock expects contracts to be renewed on a one year rolling contract basis. Such arrangements should minimize post employment expenses of the company to executives.

Where longer term contracts are entered into, or contracts are renewed for periods in excess of one year, BlackRock expects disclosure of the rationale of the justification of such approvals by the remuneration committee.

Change of control provisions

Any change of control provisions that affect the remuneration arrangements of the CEO or executives directors should be disclosed in the annual report.

BlackRock believes that the remuneration committee should have discretion in relation to change of control provisions as the circumstances that may result in a change of control are varied and cannot be determined at the time contracts are entered into.

Elements of executive remuneration

Executive remuneration will generally, but not necessarily comprise some or all of the following elements:

- Fixed remuneration

    Base remuneration

    Superannuation contributions

    Non-monetary benefits

    Leave entitlements

- Variable remuneration
    - Short term incentive (STI)
    - Long term incentive (LTI)
- Other
    - Sign-on payments
    - Retention provisions
    - Termination provisions

Fixed remuneration

Fixed remuneration should reflect the role and responsibilities of the executive role taking into account, inter alia, business and geographical complexity. When assessing the appropriateness of the level of fixed remuneration, BlackRock will use the median of the company's market cap peer group as a guide. Where a CEO's fixed remuneration is significantly above the median of the company's market cap peer group, BlackRock expects to see a cogent explanation in the annual report.

Short term incentives

STIs should be linked to performance. Disclosure in the annual report should provide shareholders an understanding of the maximum amount of STI award an executive can earn in a given year. For example, this may be expressed as a percentage of fixed remuneration.

The annual report should clearly state the performance measures and the hurdles that are required to be met for an STI to vest. BlackRock does however, accept that in the case of STIs, performance measures may involve commercially sensitive information. In such cases, BlackRock will accept non- disclosure of future performance targets, however, expects retrospective disclosure of nature of the performance measure, the performance hurdle met and the percentage of the award that vested on an annual basis.

The annual report should also explain why each STI performance measure was selected and the relationship of each performance measure to the company's stated short term strategy.

The accept should clearly disclose the performance measures that were met, the performance hurdle that was achieved and the amount of remuneration rewarded in respect of each performance measure for the CEO and executive directors.

BlackRock also encourages companies to defer a significant portion of an annual performance based award into equity which may vest over a period of around three years from grant date. Deferring a significant portion of an STI will encourage management to think beyond the initial 12 month performance period.

BlackRock is always concerned where executives appear to have been rewarded via an STI when short term performance has been prima facie poor. In such situations BlackRock expects a cogent explanation regarding why management appears to have been rewarded for poor performance. BlackRock may consider voting against the chair of the remuneration where there is a significant mismatch between performance and executive remuneration rewards.

Long term Incentives

Link between long term remuneration structure and company strategy

Blackrock expects a clear link between the structure of a company's long term incentive plans and the company's strategy. The link between executive remuneration structure and strategy should relate to the performance period and performance measures used.

Annual grants of awards

It is preferable for long term incentive awards to be granted in annual grants rather than rather than in an ad hoc manner. Annual grants allow the remuneration committee to use its discretion to amend the terms of grants as circumstances change. Exceptions may be made in start up or transformational situations where specific and highly value adding milestones can be identified. Where the remuneration committee has used its discretion to change the terms of an award BlackRock expects disclosure of why and how the discretion was used.

Performance period

The performance period chosen should be linked to the type of business and overall long term strategy. For example a company involved in the construction/operation of major infrastructure assets would be expected to have a performance period of not less than three years and preferably up to five years. For companies operating in the retails sector, where fast turnover of stock is key, BlackRock accepts a performance period of less than three years. Where a performance period for a long term incentive is less than three years, a company should provide a clear explanation for the short performance period and explain how this is linked to overall long term strategy.

Performance measures

There are many types of performance measures that can be used in a long term incentive plan. BlackRock expects to see a relationship between the performance measures chosen, the type of industry in which the company operates, the key value drivers of the business and overall long term strategy. The annual report or explanatory notes should contain clear rationale regarding why the particular performance measures were chosen and how they relate to long term strategy and key value drivers of the business.

Performance hurdle and calibration

The minimum performance hurdle that is required to be achieved before performance based awards vest should involve above median performance. Maximum awards should only vest when there has been exceptional performance. Where accounting measures such as earnings per share or return on equity have been used, the annual report should provide a clear explanation of the hurdle range that has been selected and why the range represents exceptional performance.

BlackRock believes that the use of cliff vesting (which involves a significant portion of awards vesting at a single measurement point) should be avoided unless a cogent explanation for this type of structure can be provided. In BlackRock's view awards should vest on a sliding scale to ensure management is not focused on a single performance hurdle.

Multiple performance measures

BlackRock believes that the use of multiple performance measures in a long term incentive plan will avoid focusing management on a single performance measure and hence diversify risk.

Remuneration vehicle

The remuneration vehicle is the form in which remuneration is delivered to the executive. For example it may be in cash or salary sacrifice, a type of option or other equity based vehicle.

Risk differentials of remuneration vehicles

Remuneration vehicles have differing risk profiles. For example, remuneration to be received in cash has little risk when compared with options granted with an exercise price equal to the market price of the security at grant date.

The use of remuneration vehicles such as options provides leveraged returns and accordingly, may increase management's appetite for risk beyond that expected by shareholders. Remuneration committees should ensure that the use of a particular remuneration vehicle will not result in excessive risk taking by management and should be aligned with the risk profile of the particular company and expectations of shareholders.

Options

Where options are used as the remuneration vehicle, BlackRock expects the exercise price to be at least equal to the market price at grant date. Any shareholder proposal relating to option grants should provide full details of the valuation of the grant at the date of grant.

Index linked Options

Index linked options link the exercise price to the movement of a particular index and avoid executives achieving windfall gains due to market movements and also can maintain an incentive when the overall market has a significant negative correction. Index linked options are suitable only where the company has a suitable peer group of companies in order to establish an appropriate index.

Treatment of dividends

Where an equity based remuneration vehicle has been used it is important for dividends to be taken into account in the remuneration structure. This is because management should not be influenced by the structure of their remuneration in respect of their capital management decisions. For example, if executives received options which have an exercise price equal to the market price at grant date, one way of increasing the value of the options is to not provide dividends during the performance period or undertake share buy-backs as an alternative to paying dividends.

Where an equity based remuneration vehicle has been used, dividends paid during the performance period should be held in trust until the equity vests and paid to executives on a pro rata basis in accordance with the equity that vests. The value of dividends should be taken into account when determining total remuneration.

To not take into account dividends in equity based incentive schemes may lead to sub-optimal capital management decisions.

Disclosure

BlackRock expects the annual report to provide a sound explanation for the remuneration vehicle selected and how it is related to strategy.

Types of performance measures

BlackRock believes the remuneration committee is in the best position to determine the appropriate performance measures to be used in a long term incentive plan. As discussed above BlackRock expects the annual report to clearly state why particular performance measures have been used and the link between those measures and the company's long term strategy and the performance conditions should be structured to prevent undue risk taking by executives.

The performance measures discussed below do not represent a finite list. BlackRock will consider other performance measures not discussed below on a case by case basis. In each case BlackRock will be looking for an explanation of why the measure was used and its link to long term strategy. BlackRock will support any long term performance measure where it is clear it will influence the behavior of executives to act in the long term interests of shareholders.

Share price targets/absolute total shareholder return (TSR)

BlackRock does not generally support performance measures that are based on share price targets or absolute TSR as such measures are more influenced by market forces than the contribution of the executives. These measures may also result in executives being rewarded inappropriately as a result of a general rise in the market. The opposite can also occur when there is a significant negative correction in the market and executives who may have made a considerable contribution to the long term sustainable growth of the company miss out on awards. This situation can lead to issues relating to retention and executive morale.

Relative TSR

In BlackRock's view relative TSR is only useful at measuring the performance of management when an appropriate peer group can be found. Given the size and depth of the New Zealand market it is often difficult to find an appropriate peer group with which to measure relative performance.

The use of relative TSR against a general index (eg NZSX 20) in BlackRock's view is not a particularly good measure as a company's TSR is measured against others which have differing business cycles, value drivers and many other variables that influence performance. Management has very little influence over relative TSR.

Accounting measures

Accounting measures are generally transparent and easily understood by shareholders, particularly when statutory EPS has been used.

Some companies use "underlying" or "adjusted" accounting measures such as earnings per share. These measures are appropriate where there is an element of revenue or expense which may be outside the influence of management. In cases where an adjusted accounting measure has been used BlackRock expects disclosure of the rationale behind the use of an adjusted measure as well as disclosure of the reconciliation between statutory accounting measures and the adjusted measure.

When assessing how challenging an accounting based performance hurdle is, BlackRock will take into account analyst consensus forecasts at the time the hurdle was set.

Return on equity/capital employed

Capital efficiency measures are appropriate where significant investment is required and the business is capital intensive. If capital return performance measures are used, there must be clear disclosure of the capital controls in place to avoid excessive leverage and hence risk.

Economic profit

Economic profit measures the value created in excess of the company's overall cost of capital. This measure is valid for capital intensive industries as it ensures that the cost of that capital is covered before executive awards are achieved. If used there must be assurance that there are adequate board controls to review judgments exercised for assessing the cost of capital.

Milestone or operational measures

Milestone or operational performance hurdles can encourage alignment of management's actions with the company's long term strategy. Where milestone performance measures are used BlackRock expects full disclosure of the performance measure and the performance hurdle. BlackRock does accept that some milestone performance hurdles may contain commercially sensitive information. In such cases, BlackRock expects retrospective disclosure of performance against those measures, the hurdles and the percentage of awards vesting.

BlackRock will assess the appropriateness or otherwise of milestone performance measures on a case by case basis. BlackRock will take into account the type of management behaviour that such measures may encourage. For example, if the milestone is to produce a certain quantity of ore in a particular period, BlackRock would have concerns that that this could encourage production to meet the milestone measure but ignores costs of production. Such behaviour is not, in BlackRock's view, in the long term interests of shareholders.

Earnings before interest, tax, depreciation and amortization (EBITDA)

BlackRock does not generally support the use of EBITDA as a long term performance measure unless a cogent explanation can be provided. EBITDA can be increased in the medium term through acquisitions that ignore debt and quality of acquisitions. An EBITDA measure can encourage management to take undue risk in growing EBITDA through purchasing assets that may not provide long term value to shareholders and can increase risk through excessive debt. The result in the medium term is increased EBITDA however the longer term outcome may be undue increased risk to shareholders due to non-performing assets and increased debt.

Incorporation of risk factors in remuneration structures

As discussed above, pursuant to ASX Corporate Governance Council's Principle 7 listed companies should identify, assess, monitor and manage material business risk. The outcome of sound risk management is sustainability of earnings in the long term.

BlackRock expects companies to explain the incentive framework's impact on risk. If controls are not in place to encourage sustainable performance an explanation should be provided as to why.

Where management has failed to manage identified risks, BlackRock expects to see such failures reflected in the quantum of performance based remuneration that vests in the performance period where the risk management failure occurred. Where there has been a failure to manage risk, which has resulted in the loss of shareholder value and this has not been taken into account when assessing performance based pay, we expect a cogent explanation. If the specific remuneration structure does not incorporate risk then the remuneration committee should have discretion to reduce the level of performance based pay when there has been a failure by management to manage key risks.

The type of risks that BlackRock expect to see taken into account in remuneration structures would include, but are not limited to, safety and implementation and maintenance of information technology systems.

Where an earnings based performance measure has been used, BlackRock expects companies to disclose how identified risks are managed and not subject to cost cutting in order to increase the performance measure and accordingly performance based pay and leave the company exposed to unmanaged risks.

Sign-on awards

In cases where a newly appointed executive has forgone remuneration from a past employer in order to take on a new role, a company may reimburse the new executive by way of sign-on remuneration. Where such remuneration has been made BlackRock expects full disclosure of the quantum paid. BlackRock also prefers such remuneration to have an equity component and at least a portion to be subject to some sort of time vesting conditions.

Retention payments

Where the CEO's and/or executive director's contracts have provision for a retention payment, the annual report should provide full disclosure of such commitments. BlackRock prefers to see retention payments with an element of equity.

Termination payments

Executive contracts should not be structured in such a manner as to allow for large payouts as a consequence of poor and inadequate performance.

BlackRock prefers to see termination payments provisions that do not exceed one year's level of fixed remuneration unless a cogent explanation has been provided. Further, BlackRock believes any early vesting of performance based securities in the event of termination, should be subject to the stated performance conditions and vest on a pro rata basis.

Post employment and good leavers

BlackRock encourages incentive plans that ensure executives remain accountable for their legacy in the event they leave. Providing an executive is a good leaver, BlackRock would expect that long term plans, in particular, remain "live", and are tested as usual at the end of the stated performance period. It is believed that such arrangement ensure the selection and development of effective successors.

Retesting

In BlackRock's view a well structured long term incentive plan that has well chosen performance measures, appropriate performance hurdles and involves annual grants of equity should not require retesting provisions.

However, Blackrock will assess retesting provisions on a case-by-case basis. Generally BlackRock does not support a regime of continual retesting as this may distract management from a longer term focus.

Hedging of securities

Given the nature of the role of the CEO and executive directors and their access to information, in BlackRock's view it is inappropriate for executives to enter into hedging arrangements relating to their direct and indirect shareholdings as well as any unvested performance based equity remuneration.

As mentioned above, in certain circumstances BlackRock believes the CEO and executive directors should disclose shares subject to margin calls.

Dilution

NZSX Listing Rule 7.3.6 limits employee share plans to3% of capital unless shareholder approval is obtain. Where a company seeks shareholder approval to increase the 3% limit BlackRock will take into account the structure of the plan and its potential impact on shareholder value in the long term. Explanatory notes accompanying such proposal should provide a detailed description of the plan and the rational for the increased limit.

Disclosure of equity based LTI's

To allow BlackRock to compare remuneration practices of the companies in which we invest we expect disclosure in respect, of the CEO and each executive director, of the fair value at grant date of all equity based remuneration grants.

Requests for approval of equity grants

NZSX Listing Rule 7.3.1 requires shareholder approval of dilutionary equity grants to directors. The explanatory notes accompany such proposals should provide full details of the director's remuneration package including fixed remuneration, short and long term incentives as well as termination provisions. Without this information BlackRock may be unable to support the proposal.

Approach to assessing remuneration policies of smaller companies

Listed on the NZSX are companies that are in an exploration/evaluation/development phase. Often the only revenue is interest and such companies often have a high cash burn rate. It is unreasonable to expect these companies to have remuneration structures that incorporate accounting performance measures and relative return measures. BlackRock will assess the remuneration policies of these companies on a case by case basis with the focus taking into account the particular phase the company is in, the quantum of remuneration paid to executives and non-executive directors and the potential for unreasonable dilution of shareholders' equity. As these companies move into a production phase BlackRock expects to see remuneration practices to evolve to reflect the change in operational status of the company.

Social, ethical and environmental issues (SEE)

Disclosure of material SEE risks

BlackRock expects listed companies to disclose all material non-financial risks relating to SEE issues as per above, in the annual report.

Engagement

Where BlackRock believes management of a material SEE exposure appears to be inadequate we will endeavor to raise our concerns directly with the company. If our engagement efforts are unsuccessful then the next mechanism available to us is to vote against the re-election of directors deemed responsible for any potential harm to shareholders' interests. When there has been failure to manage material SEE risks and this has resulted in an event that has materially harmed shareholder value, BlackRock may consider voting against the directors responsible.

General corporate governance matters

Amendments to constitutions

These proposals vary from routine changes to reflect up-dates to the Corporations' Act, Listing Rules and other regulatory revisions to significant changes that substantially change the governance of the company. BlackRock will review such proposals on a case by case basis and support those that we believe are in the best interests of shareholders.

Bundled proposals

We believe that shareholders should have the opportunity to review substantial governance changes individually without having to accept bundled proposals. Where several measures are grouped into one proposal, BlackRock may reject certain positive changes when linked with proposals that generally contradict or impede the rights and economic interests of shareholders.

Reincorporation

Proposals to reincorporate from one state or country to another are most frequently motivated by considerations of anti-takeover protections or cost savings. Where cost savings are the sole issue, we will typically favour reincorporation. In all instances, we will evaluate the changes to shareholder protection under the new charter/articles/by-laws to assess whether the move increases or decreases shareholder protections. Where we find that shareholder protections are diminished, we will support reincorporation if we determine that the overall benefits outweigh the diminished rights.

Shareholder proposals

Whilst we recognize the importance of the right of shareholders to submit proposals to the general meeting, we will not support those that are frivolous or that cover an issue that we believe the board or management is or has addressed adequately. We will support shareholder proposals that we believe enhance shareholders' rights or are in the economic interests of shareholders.