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INVESTMENT STEWARDSHIP REPORT: AMERICAS

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Contents

The BlackRock Investment Stewardship (BIS) team publishes quarterly reports to explain BlackRock's approach to corporate governance engagement that supports long-term value creation for our clients. The examples reported give a sense of the wide range of issues our engagements and voting analyses cover. We aim to provide examples that highlight particular environmental, social and governance ("ESG") considerations, emerging practices or issues and notable company-specific developments. We also provide examples of our engagement in the public domain, such as responses to formal policy consultations and presentations or informal discussions at conferences.

Engagement and Voting Highlights

This quarter, the Americas Investment Stewardship team's engagements and voting activities spanned a number of key topics, ranging from board oversight and quality, corporate culture and strategy, environmental risks and opportunities, and human capital management. We were also involved in several ongoing contested situations. The following examples provide insight into these activities and their outcomes.

Value creation in the technology sector: a reverse merger transaction

1 In the third and fourth quarters of 2018 we engaged with a private technology company where we held two of its publicly listed stocks, one of which tracked the performance of the other public stock. Because of the company's unusual stock structure, our initial engagements focused on the private company's attempts to improve on its existing corporate structure. In our engagements, we discussed the possibility of the private company entering the public market as a solution.

After weeks of discussion, the private company decided that the best method for entering the public markets was through a reverse merger transaction, where shareholders of the tracking stock would swap their shares for newly created public stock that would then trade freely. The company determined that a traditional initial public offering (IPO) was not the best course of action due to the length of time this might require and because of concerns over a lower valuation for the company.

BIS along with members of several active investment teams at BlackRock engaged with management of the private company, various external advisors of the private company, and the two public companies to discuss the terms of the proposed transaction. We also shared our views on the private company's governance and potential valuation with relevant stakeholders. In August 2018, the public company tracking stock issued a proxy statement detailing the process undertaken by the special board committee to evaluate the proposed transaction.

Unfortunately, the company's proxy statement revealed a less than robust negotiation process between the tracking stock's special committee and the private company. When we spoke with the private company, we expressed our reservations with their terms, citing in particular their (1) heavily diminished stock price, and relatedly, (2) our view that the company had severely undervalued its potential worth in the public market. In this round of negotiations the private company did not consider amending its terms. We, therefore, did not support the transaction, as it would not have delivered fair value to shareholders.

As time passed, sentiment against the transaction spread to other institutional shareholders. In subsequent dialogue, BIS continued to convey to the company and its advisors that they should improve the offer. We also suggested adding a board seat to be filled by a director elected by the independent shareholders to improve the company's governance.

After months of discussion and continued concerns expressed by shareholders about the price of the tracking stock, new terms were formed, which BlackRock supported. Under the new agreement, shareholders would still trade their shares in the tracking stock for shares of the company in the public market, but would receive greater value. The revised deal provided a $5 billion overall value-add when compared to the original valuation. Additionally, the company also agreed to appoint a new independent board member. The shortcomings of the early offer became particularly evident in the wake of the revised deal.

Our engagements and the resulting value-add to this reverse merger transaction underscores BIS' role as part of BlackRock's investment function. In its fiduciary capacity to engage both internally with

BlackRock's various investment teams and externally with companies, BIS can improve the terms offered to shareholders, such as BlackRock's clients, in such transactions and promote governance enhancements.

Cybersecurity engagements: lessons learned

2 Data security issues and cybersecurity concerns have grown as companies have access to, and responsibility for, more private information. Data security breaches and hacks have occurred at companies of all sizes across all sectors. Most companies recognize the importance of implementing management best practices to reduce the likelihood of a cyberattack or a data security breach. Such practices can not only reduce the odds of an incident occurring, but can limit the scope of the ensuing financial, competitive, and/or reputational damage that may result from a breach.

We engaged with several companies that had experienced cyber-attacks which, to varying degrees, exposed sensitive customer data to the public and malicious actors, interfered with manufacturing and research and development processes, and disrupted sales operations. In each instance, the breaches resulted in material financial losses to the companies in the form of civil lawsuits, production shutdowns, and/or reduction in sales. During our engagements, we have discussed governance, strategy, and risk management around cybersecurity threats and data security issues. Broadly speaking, over the course of these engagements, we have learned that a company's approach to managing data security depends on factors specific to that company's individual business – i.e. the nature of its products and services, industries, geographical footprint, competitive differentiators, and strategic direction.

One insurance company that we engaged subsequent to a significant patient data breach shared how they had transformed their oversight of cyber risks and allocated a large increase in resources to address prevention efforts for the future. In addition to recently adding a new director with a technology background, every director has undertaken training to expand their knowledge of cybersecurity issues. Now, the full board oversees the company's cybersecurity strategy. In this capacity, the topic is discussed at every board meeting and board members engage annually with an independent expert firm to review the company's oversight strategy.

We also engaged with a pharmaceutical company where we discussed key takeaways from its recovery and remediation process following a cyber-attack which disrupted their global operations. Following the incident, the board partnered with a cybersecurity technology firm that assessed their internal controls and explored strategies for improving data protection. The board enhanced its approach to crisis management, developing clear lines of responsibility and oversight and direct channels for regular communications. The company explained that these processes were established in order to quickly mobilize collective action across the firm.

We also engaged a company that spoke about the need to improve employee vigilance around cyber issues, and simultaneously create incentives to remain engaged and watchful. Separately, we engaged a number of utility companies on these risks. It was interesting to learn how sector cybersecurity sharing groups are helping companies to better understand areas of weakness and how collective industry-led action can assist with resilience.

Overall, several key messages emerged from these various engagements:

- Companies are seeking to expand director experience or retain outside consultants with specific skills in data security and information technology.
- Data security and cyber risk needs to be overseen by the board of directors.
- Strategies for mitigating cyber risks can be both preventative and remedial in nature, and while risk cannot be eliminated, preparedness can reduce the scope of potential financial impacts to companies.
- Fostering strong internal partnerships and a culture of diligence is critical.

BIS views data security and cybersecurity as significant enterprise-level risks that can impact all levels of a company's operational activities. We will continue to engage with boards and management to understand how practices are evolving.

Human capital management consulting in healthcare: driving long-term value

3 Within the industrials sector, there exist a handful of consulting firms that cater to specific industries like education, healthcare, and infrastructure. As consultants, they offer a variety of services, including providing external perspective on the importance of human capital management (HCM) in the context of a company's long-term outlook.

BIS recently engaged with a public healthcare-oriented consulting firm that provided us with insight into their HCM practice and how they had to expand their own expertise in this area given these demands in the healthcare industry. Like any business, healthcare is transactional in nature, constrained by time and resources. The firm's directors explained that, while patients may receive the same diagnosis, surgery, or consultation from a variety of hospitals or specialists, "personal care" (or the "human element") is critical to a successful recovery and patient experience, and therefore a material issue in the business.

During our engagement we discussed the two-pronged impact that high quality personal care has on long-term value creation. On one hand, when patients feel that their needs are adequately addressed and their healthcare providers are attuned to their concerns, litigation risks decrease. On the other hand, when employees - doctors, nurses, and other care providers - operate in an environment that empowers staff of all levels to speak up, make suggestions, or ask for clarification, morale powers efficiency and reduces accident rates. Thus, a positive culture impacts both the bottom line and patient health.

Consequently, the consulting firm expanded its employee expertise and solutions offerings. However, contrary to business improvements a company might make through purchasing technology or lowering input costs, changing culture takes time. On a quarterly, or even yearly basis, it may be difficult to judge the progress of a culture change. BIS continues to engage with companies in similar situations on the underlying business implications of HCM to better understand how best practices can effectively create long-term value, while companies engage their workforce to strengthen one of their most valuable assets - employees.

A proxy contest in the consumer staples industry

4 In the context of an activist campaign, BIS engages companies with the goal of understanding a company's go-forward strategic direction, as well as its specific responses to the criticisms raised by activists. This entails gaining a better understanding of a company's financial performance and governance practices. As part of our due diligence, we engage with the company's board and management as well as the activist(s) and their director nominees, often multiple times with each side(s). Although each situation is unique, our vote is determined by our assessment of which outcome best aligns with the economic interests of our clients, many of whom are long-term investors who will hold shares in a company well after most activist positions have been sold. Part of this assessment is the feasibility of the proposal for change, management and the board's performance track record and willingness to change, as well as our historical engagements with the company.

In the fourth quarter, an activist hedge fund took a stake in a global food company and publicly campaigned for board overhaul and internal policy changes. The activist argued that they could refresh what they perceived as an entrenched board and improve governance practices to enhance the company's strategy and performance.

In our discussions, the activist expressed particular concerns vis-à-vis the company's strategic direction. The activist discussed the stock price decrease for the year, poor due diligence efforts, operational lapses with major customers (i.e. significant product recalls), and poor succession plans for replacing their CEO who had recently retired.

We discussed with the company proposed governance enhancements and business strategy moving forward. After thorough analysis and multiple meetings with both parties, we decided that change was in fact warranted and could be achieved through appropriate board refreshment. We felt that a compromise could be reached between the two parties that would satisfy all stakeholders.

The activist and the company negotiated further, and eventually the activist agreed to reduce its proposed director slate, ultimately making an agreement with the company to:

1. Add two independent nominees to the board
2. Provide input on the addition of a third board member in 2019, and
3. Offer advice as the company searches for a new CEO

The relatively quick settlement meant reduced costs and diminished distractions for the management team. It also enabled an appropriate level of incremental change to the company's board, leading to the potential for governance changes and the potential for gains in long-term value. We view the fairly speedy settlement as a win for shareholders.

Engaging at the intersection of sustainability and finance

4 In last year's Q4 2017 quarterly report we wrote about our efforts engaging with insurance companies on climate risks and opportunities. We continue to engage with financial institutions on this issue and, in the fourth quarter, we spoke with a number of U.S. banks regarding the impact of climate-related risks to their business operations.

One bank explained how it had integrated climate risk into its business strategy and reporting by setting targets related to their environmental financing, as well as the firm's environmental and social risk management. The company discussed how they are assessing their own environmental footprint and their goal to power 100% of their operations with renewable energy by 2020.

To complement these efforts, the company committed to implementing the recommendations set forth by the G20 Financial Stability Board's Task Force on Climate-Related Financial Disclosures (TCFD). In partnership with the United Nations Environment Programme - Finance Initiative (UNEP FI), the bank also participated in a climate scenario analysis pilot project to learn about financial risks and opportunities related to climate change on lending portfolios in the oil, gas, and utilities sector. Subsequently, the company published its analysis and disclosures in alignment with the TCFD.

We engaged with two additional banks around their efforts to implement the TCFD recommendations. The first company is focused on assessing climate risk in its consumer lending portfolio that will lead to a white paper in which they detail their findings. The second company highlighted their commitment to facilitate $200 billion in clean financing through 2025, and discussed plans to issue a standalone report in line with TCFD recommendations. We were encouraged to hear both companies emphasize board and senior management involvement in overseeing these initiatives.

We will continue to engage with companies in the financial sector to identify best practices and encourage continued analysis and disclosure of these risks and opportunities.

Engagement and Voting Statistics

Americas Engagement Statistics[1]

	Level of Engagement[2]			Topics Discussed*		
Number of engagements	Basic	Moderate	Extensive	Environmental	Social	Governance
241	154	75	12	63	43	241

*Most engagement conversations cover multiple topics. Our engagement statistics reflect the primary engagement topic that formed the basis for the meeting request.

Americas Region Voting Statistics[1]

Country	Number of meetings voted	Number of proposals	% of meetings voted against one or more management recommendations	% of proposals voted against management recommendation
USA	410	3,121	20%	6%
Canada	18	150	37%	7%
Latin and South America	68	393	35%	15%
Americas Region Total	496	3,664	23%	7%

[1] The Americas engagement statistics are sourced from BlackRock and the voting statistics are sourced from ISS Proxy Exchange on January 5, 2019 and both are a reflection of 4th Quarter 2018.

[2] Basic engagement is generally a single conversation on a routine matter; Moderate engagement is technically more complex and generally involves more than one meeting; Extensive engagement is technically complex, high profile and involves numerous meetings over a longer time frame. Source: BlackRock as of 4th Quarter 2018.

Responsible Leadership

Awards

In December, BIS was awarded the International Corporate Governance Network (ICGN) *Global Stewardship Disclosure Award for Asset Managers*. We view transparency as a key component of our investment stewardship activities and therefore provide detailed reports on our website, including global engagement principles, regional proxy voting guidelines, quarterly and annual reports, position papers and commentaries, and vote bulletins.

In November, BIS was honored by 2020 Women on Boards and its Bay Area affiliate How Women Lead with the *Disruptor Award*, acknowledging our work around increasing board diversity, including the number of women directors on boards. As mentioned earlier this year, we identified approximately 300 U.S. companies in the Russell 1000 as candidates for engagement on board diversity and wrote to each company explaining our views on the issue. We have had productive conversations with 160 companies through the end of the fourth quarter. Board quality and diversity remain a focal point of many of our engagements, and we will continue to engage with these companies to assess their progress.

Speaking Events

Members of the Americas BIS team spoke at or participated in a number of events over the past quarter, with the goal of furthering discussion on matters deemed important to investors and/or promoting an increased understanding of BlackRock's approach to investment stewardship. We prioritize events that enable us to connect with key constituents and thought leaders, including corporate directors, senior members of management teams, and other shareholders, including clients.

Carolina Directors Exchange – Charlotte, NC

In October, we participated in a panel interview entitled "Keeping Your Board Relevant". We discussed the evolution and role of BIS, Larry Fink's annual CEO letter, our engagement priorities, characteristics of a typical engagement, and how engagements inform our voting decisions. The event provided an opportunity to share our work and governance positions with a group of regionally-based public company directors.

NASDAQ Board Leadership Forum – New York, NY

We spoke on a panel on shareholder engagement, explaining what investment stewardship means at BlackRock, and specifically how and when we engage with activist investors. Participants included corporate executives, board directors, general counsel and other investment and governance professionals.

BAML Future of Financials Conference – New York, NY

In November we spoke on a panel alongside an activist hedge fund and investment bank advisor. The discussion focused on BlackRock's engagement approach during activist situations, the evolution of the BIS team, characteristics of an engagement, and differing industry definitions of "long term."

G100 Board Excellence – Menlo Park, CA

We spoke on a panel which examined how boards could identify their potential vulnerabilities and take proactive action in the face of activist campaigns. We discussed how boards should engage with investors like BlackRock, representing long-term capital, as we seek greater insight into corporate strategies and the board's effectiveness in holding management accountable. The audience included Global Fortune 100 directors, general counsels, and other governance thought leaders.

PwC Governance Insight – New York, NY

We spoke on a panel entitled "Investors Voices: Exerting Influence in the Boardroom." The audience consisted of seasoned board directors from across sectors. The event offered us an opportunity to provide context to Larry Fink's 2018 letter to CEOs, highlight key governance factors and how we evaluate them, share our views on board composition and diversity, and explain our engagement-first approach.

Market Developments and Trends

U.S. Securities and Exchange Commission (SEC) Staff Roundtable

In November, the SEC hosted a Staff Roundtable on the Proxy Process with various stakeholders in order to provide the Commission with perspectives on existing regulations and processes related to shareholder engagement. The roundtable explored various topics within the proxy ecosystem, encompassing the voting process, shareholder proposals, and the role of proxy advisory firms. In advance of the roundtable, BlackRock published a *ViewPoint* and submitted a comment letter to the SEC outlining our perspective on the issues. BIS participated in this public event and emphasized BlackRock's support for efforts to enhance the transparency of the proxy voting process.

MSCI – treatment of companies with differentiated voting rights

In 2018, MSCI launched a consultation regarding the treatment of companies with unequal voting structure in MSCI Equity Indexes. Our open letter response to this consultation shares our view that "one share, one vote" is the preferable structure for publicly-traded companies. We recognize the potential benefits of dual class shares to newly public companies as they establish themselves, however, we believe that these structures should have a specific and limited duration. We believe that regulators in conjunction with listing exchanges should be the arbiters of corporate governance standards for publicly listed companies.

We were encouraged that in October MSCI decided not to change its methodology in alignment with our recommendation, allowing for companies with unequal voting structures will remain eligible for inclusion in MSCI indexes.

Separately, in October an investor group including BlackRock petitioned the New York Stock Exchange and NASDAQ asking the exchanges to amend their listing standards regarding unequal voting right structures. According to the petition, public companies listing with multiple share classes should convert their share structure within seven years of the initial public offering to a 'one share, one vote' structure

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