BLACKROCK®

April 19, 2018

Mr. Baer Pettit
President
MSCI, Inc.
Ten Bishops Square, Ninth Floor
London E1 6EG United Kingdom

Re: Open Letter Regarding Consultation on the Treatment of Unequal Voting Structures in the MSCI Equity Indexes

Dear Mr. Pettit:

BlackRock, Inc. (together with its affiliates, "BlackRock") appreciates the opportunity to comment on MSCI's *Consultation on the Treatment of Unequal Voting Structures in the MSCI Equity Indexes*.[1] As one of the world's leading asset management firms, BlackRock manages assets on behalf of institutional and individual clients worldwide, across equity, fixed income, liquidity, real estate, alternatives, and multi-asset strategies. Our client base includes pension plans, endowments, foundations, charities, official institutions, insurers and other financial institutions, as well as individuals around the world.

BlackRock is a strong advocate for sound corporate governance practices at publicly traded companies in which we invest on behalf of our clients, and for the preservation of investor rights. We, therefore, appreciate MSCI's attention to the issue of unequal voting rights in publicly traded companies, as these structures reduce the rights of shareholders. **However, we believe policymakers, not index providers, should set corporate governance standards.** While the objectives of MSCI's proposal are aligned with our view that "one vote for one share" is the preferable structure for publicly-traded companies, we believe that an alternative approach would be more effective in achieving this objective while avoiding the significant changes to existing MSCI broad market indexes that would be required to effectuate MSCI's proposed solution.

In our view, broad market indexes should be as expansive and diverse as the underlying industries and economies whose performance they seek to capture. In constructing indexes, index providers should make every effort to reflect the investable marketplace in the broad benchmark indexes that they produce. In addition to limiting the opportunity set for index investors, the proposed changes will be costly for investors in index products that reference these indices, and these costs would be incurred for changes not related to accurate representation of the investable universe (See Appendix). For example, the turnover in ACWI, Emerging Market, and US Indexes would each result in billions of dollars of trades to adjust to the new index weightings. And in some markets, such as the UAE Index, close to 25% of the market value will be deleted from the existing index.

---

[1] MSCI, Consultation on the Treatment of Unequal Voting Structures in the MSCI Equity Indexes (Jan. 2018), available at https://www.msci.com/documents/1296102/8328554/Consultation_Voting+Rights.pdf/15d99336-9346-4e42-9cd3-a4a03ecff339.

We recommend that MSCI pursue an alternative approach that would allow index investors to choose between (i) broad market indexes that reflect the investable universe and (ii) indexes that have alternative weightings or screen companies based on governance principles, similar to index offerings with tobacco or social screens. This solution would allow investors who feel strongly about corporate governance issues to "vote with their feet" without creating the market disruption or transaction costs associated with the proposed approach.

We believe that the context for our views on MSCI's proposal is important. Therefore, we have sought to first stake out some broad principles that BlackRock believes are important in relation to any discussion about dual share class (or weighted voting rights) companies.

BlackRock's Philosophy on Corporate Governance

We believe that certain fundamental rights should be attached to share ownership. Companies and their boards should be accountable to shareholders and structured with appropriate checks and balances to ensure that they operate in shareholders' interests. Studies have shown that good corporate governance contributes to improved corporate performance and accountability in creating long-term shareholder value for publicly traded companies[2]. The guiding principles to ensure strong corporate governance, include board accountability to shareholders, development of an independent leadership structure, and voting rights in proportion to shareholders' economic interest – in other words, "one share, one vote".

Effective voting rights are central to the rights of ownership and we believe strongly in one vote for one share as a guiding principle that supports good corporate governance. Shareholders, as the residual claimants, have the strongest interest in protecting firm value, and voting power should match economic exposure. It is at the core of corporate governance that to reduce the agency problem, all shareholders need to effectively monitor companies. Shareholders should have the right to elect, remove and nominate directors, approve the appointment of the auditor and to amend the corporate charter or bylaws. Shareholders should be able to vote on matters that are material to the protection of their investment including but not limited to changes to the purpose of the business, matters related to capital issuance such as dilution levels and preemptive rights, the distribution of income and the capital structure.

BlackRock's View on Dual Share Class Listings

We are concerned that the creation of a dual share class may result in an over-concentration of power in the hands of a few shareholders, thus disenfranchising other shareholders and amplifying the conflict of interest, which the one share, one vote principle is designed to mitigate. As such, we are concerned that dual class structures call into question a fundamental tenet of good corporate governance and undermine the efforts to improve the quality of investor stewardship, potentially making such structures less than ideal for investors. As regulators call on investors to further engage with issuers in a deeper and more responsible way, we believe they equally should protect shareholders' rights, particularly those of minority shareholders, by promoting the one share, one vote principle.

---

2 For a review of the academic literature, see Inessa Love, *Corporate Governance and Performance around the World: What We Know and What We Don't*, World Bank Research Observer, Vol. 26, Issue 1 (2011), available at https://elibrary.worldbank.org/doi/pdf/10.1093/wbro/lkp030.

While our preference is for one share, one vote companies, we recognize that in certain circumstances, there may be a valid argument for dual-class listings, at least for a limited period of time. We also recognize that dual share class structures are not “new” and in fact have been used for many decades. The proponents of dual class shares make the argument that unequal voting rights allow entrepreneurial founders to retain control and invest for long-term results without being exposed to outside pressure to maximize short-term results. **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.**[3] We recommend that companies incorporate sunset provisions based upon time or a triggered event to eliminate unequal share classes. Alternatively, companies could put their company capital structure to a vote of all shareholders every 5 to 10 years. The latter approach would give the company and shareholders the ability to review and discuss the merits of maintaining the structure or converting to a single share class. We note that each of these solutions would balance companies’ needs to focus on the long-term with shareholders’ needs for accountability.

Roles and Responsibilities of Various Stakeholders

Within this discussion, it is important to remember that there are multiple stakeholders, each with an important role to play. For example, stock exchanges, market regulators, global policy bodies, publicly listed companies, asset managers, end-investors, and index providers have roles to play in the discussion. Two of the global policy bodies that have been involved in corporate governance issues are International Organization for Securities Commissions (“IOSCO”) and Organization for Economic Co-operation and Development (“OECD”).

We believe that regulators in conjunction with listing exchanges should be the arbiters of corporate governance standards for publicly listed companies. Ideally, exchanges would limit the use of dual share class structures and market regulators would mandate minimum listing standards. However, we recognize that competitive pressures may discourage these stakeholders from imposing standards that would create an uneven playing field across jurisdictions. In fact, we are concerned that the current system will lead to a race to the bottom as exchanges compete for listings by lowering their standards for corporate governance. **In light of this collective action problem, a global agreement is necessary to establish minimum corporate governance standards that would ensure a minimum level of investor protection.** We believe a global body such as IOSCO is well positioned to establish global guidelines for listing standards that could then be translated into national regulation. While we recognize that individual countries are not required to implement global standards, the introduction of global principles has worked well in the past to establish a benchmark that creates a level playing field for regulation that is in the best interests of end-investors.

---

[3] Looking over 35 years of data, a research found that “at the time of the IPO, dual class firms tend to have higher valuations than single-class firms, which valuation premium dissipates over time and turns into a discount about six years after the IPO.” See Martijn Cremers, Beni Lauterbach, and Anete Pajuste, *The Life-Cycle of Dual Class Firms*, European Corporate Governance Institute (ECGI) - Finance Working Paper No. 550/2018 (2018), available at https://ssrn.com/abstract=3062895. Harvard Law School professor Lucian Bebchuk also argues that “as time passes, the potential costs of a dual-class structure tend to increase and the potential benefits tend to erode”. See Lucian A. Bebchuk and Kobi Kastiel, *The Untenable Case for Perpetual Dual-Class Stock*, Virginia Law Review, Vol. 103, (Jun. 2017), available at https://ssrn.com/abstract=2954630 at 585-631.

In our view, the role of index providers differs significantly from the role of exchanges and regulators. Specifically, the role of index providers is to provide indexes that reflect the investable universe that the index seeks to represent, as well as offer more specialized indexes that reflect investor preferences. Index providers can support efforts to promote good governance by creating alternative indexes that incorporate corporate governance screens, such as alternative weightings or exclusion of companies with unequal voting rights, following a similar approach to index offerings with tobacco or social screens. This solution would allow investors who feel strongly about corporate governance issues to "vote with their feet", while allowing other investors who prefer their broad market index investments to reflect the investable universe to continue to do so. In addition, this approach would avoid the market disruption or transaction costs associated with reconstituting the broad market indexes.

In summary, **policymakers, not index providers, should set corporate governance standards.**

BlackRock's View on MSCI's Proposal

We believe index providers should make every effort to reflect the investable marketplace in the broad market indexes that they produce. In our view, broad market indexes should be as expansive and diverse as the underlying industries and economies whose performance they seek to capture. This inclusive approach better facilitates investors' use of benchmark indices and aligns with the diversity of objectives across public equity investors. BlackRock recommends that MSCI continue to include securities with unequal voting rights at the current weights. In addition, we recommend MSCI offer a range of bespoke indices, some of which may include or exclude certain securities across a variety of financial characteristics and/or environmental, social and governance factors, thus allowing investors to reflect their individual preferences. Furthermore, BlackRock recommends that the index providers as well as asset managers and end investors petition IOSCO to engage in a project whereby IOSCO would establish minimum corporate governance standards for companies to be eligible for public listing regardless of the jurisdiction of the exchange.

****

We thank MSCI for providing BlackRock the opportunity to comment on the MSCI's *Consultation on the Treatment of Unequal Voting Structures in the MSCI Equity Indexes*. Please contact the undersigned if you have any questions or comments regarding BlackRock's views.

Sincerely,

Barbara Novick
Vice Chairman

Appendix: Transaction costs and liquidity implications

Under MSCI's proposed change to exclude or down-weight company stocks based on weighted voting rights, investors will experience transaction costs and liquidity challenges upon implementation of these changes. To put this in perspective, below are a few of the practical impacts of MSCI's proposed change:

- Lowering weights of securities with unequal voting shares will lead to two-way turnover of 8.5% and 10.7% for the ACWI and Emerging Market Indices, respectively. The weight of Facebook in the MSCI USA Index would drop 1.15%, resulting in an estimated $5 billion sell trade in the market across indexers over two days.
- Deleting securities with zero voting power will lead to 11 deleted securities. The largest is Emirates Telecom Group, which represents 23.3% of the UAE index.
- Reinvestment of sale proceeds in illiquid markets will be challenging, leading to multiple days of trading and ticketing costs.