

31 May 2018

MSCI Equity Index Committee
7 World Trade Center
250 Greenwich Street
New York, NY 10007

Via email: clientservice@msci.com

Consultation on The Treatment of Unequal Voting Structures in the MSCI Equity Indexes

Dear Committee Members,

The Australian Council of Superannuation Investors (ACSI) is pleased to respond to MSCI's *Consultation on The Treatment of Unequal Voting Structures in the MSCI Equity Indexes* dated January 2018.

About ACSI

Established in 2001, ACSI exists to provide a strong, collective voice on environmental, social and governance (ESG) issues on behalf of our members. Our members include 38 Australian and international asset owners and institutional investors. Collectively, they manage over \$2.2 trillion in assets. Our members, either directly or via their funds managers, are major clients of MSCI and many use your index products as well as your ESG research.

ACSI members believe that the formal and informal ownership rights that accrue to investors (including voting rights and the ability to engage with investee companies) have genuine economic value, and their exercise can materially improve investment outcomes. The current consultation, and MSCI's subsequent approach to unequal voting structures, is therefore of critical importance.

Our policy on unequal voting rights

As a representative of long-term investors, ACSI believes that companies and the operation of financial markets should not erode ownership rights by disenfranchising shareholders or inhibiting their participation in company meetings.

ACSI therefore supports a "one share, one vote" capital structure¹ because this is the optimal method of empowering shareholders and aligning their interests in a company. This is fundamental to the very definition of equity securities and is not merely a governance preference.

Specifically, we are opposed to unequal voting rights structures, because they:

- separate economic ownership from voting power and disenfranchise shareholders,
- erode board and management accountability to shareholders, and
- entrench management and certain shareholders, thereby creating long-term inefficiencies and weakening the market for corporate control.

¹ [ACSI Governance Guidelines](#), November 2017, page 21.

A comment on the index providers' role

It is entirely appropriate and welcome that index providers like MSCI are taking a leadership role on this topic and considering the views of their investor clients and broader market participants. MSCI already filters and adjusts the full market for issues like size, free float, liquidity and local market structure and we see no reason why a fundamental issue for equities like voting rights should be ignored. We see index providers as a bulwark against the distressing 'race to the bottom' in corporate governance regulations and exchange rules driven primarily by competition for IPOs.

Our response

We strongly support the proposal to retain stocks with unequal voting rights in the MSCI Equity Indexes and adjusting the weights of these stocks (including to zero) to reflect the company level listed voting power. It adequately balances the need to retain broad coverage while recognizing that companies with unequal voting rights should be weighted down.

However, we feel the proposal should be strengthened in the following ways:

- **MSCI should match S&P's market leading position whereby companies with unequal voting rights will not be added into major indices.** This requirement would send a strong and appropriate message to IPO prospects that public markets investors demand 'one share, one vote' structures.
- **Companies that restrict the ability of certain share classes to elect directors should be considered as having zero votes per share.**²The ability to elect directors is an essential shareholder voting right. Without this, the market for corporate control is fundamentally weakened because acquiring a majority of the economic interest does not give the ability to effectively take control of the board and company.

We have included answers to consultation questions in the Appendix below.

Conclusion

We will be following the progress of the consultation with interest and would be happy to answer any questions the Committee may wish to raise regarding our submission. Please contact me or Mike Harut, *Manager, Equities Research and Engagement* (mharut@acsi.org.au) if you wish to discuss our submission further.

Yours sincerely,



Edward John, Executive Manager, Governance, Engagement and Policy

² At the very least, companies that place restrictions on the election of directors should only be included where the acquisition of a majority of the economic interest still gives effective board control. (Companies like those in the 'type 1' list on page 25 of the consultation paper could theoretically have this characteristic.)

Appendix: Answers the consultation questions

Below are answers to the specific questions in the consultation paper.

Question	Response
Do you agree that unequal voting shares should remain eligible for index inclusion?	As discussed above, companies already in the MSCI Equity Indexes should be subject to the method proposed, but prospective entrants should only be included where they have equal voting rights.
Do you agree that the index weight of securities with unequal voting structures should be linked to voting power?	Yes.
Is it appropriate to delete securities with zero company voting power from the MSCI Equity Indexes? (An alternative could be to maintain such securities in the indexes at very reduced weights (e.g., using 10% of the securities' free float))	Yes.
Is the application of a voting power adjustment an appropriate way to reflect misalignment between voting power and economic interest?	Yes.
Is the method for calculating the adjustment adequate?	Yes. As noted above, we strongly disagree with the exception for restrictions on director elections.
Do you agree that the votes per share should be zero in cases where voting rights are restricted? (page 10)	Yes.
Do you agree with the proposed exceptions? (page 10)	Yes. However, as noted, we strongly disagree with the exception for restrictions on director elections.
Is it appropriate to grant a grace period for current constituents?	Yes.
Is a three-year grace period sufficient or should more time be given?	Yes, three years is appropriate. It may be appropriate to extend this grace period to companies that establish sunset provisions which automatically collapse their share structure to equal voting rights after a predefined period (that cannot be extended).
Are the proposed index maintenance rules for the Vote Adjusted Security Free Float appropriate?	We have no immediate concerns.
Should MSCI implement the changes for current index constituents in one step or would a multiple step transition be appropriate?	We don't have any comment on this issue.