



**2020**

PROXY PAPER™

# GUIDELINES

AN OVERVIEW OF THE GLASS LEWIS APPROACH TO PROXY ADVICE

# PHILIPPINES



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# Guidelines Introduction

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## REGULATIONS AND GOVERNANCE CODE

Philippine corporate governance has been primarily based on the following: (i) the Revised Corporation Code of the Philippines (the “Revised Corporation Code”); (ii) the Securities Regulation Code (the “SRC”); (iii) the Philippine Stock Exchange Listing Rules; (iv) the 2017 Code of Corporate Governance for Publicly-Listed Companies (the “Code”), a combination of mandatory and voluntary best practices released by the Securities and Exchange Commission (“SEC”); and (v) the Corporate Governance Guidelines for Companies Listed on the Philippine Stock Exchange (the “CG Guidelines”) released by the Philippine Stock Exchange (“PSE”).

In late 2016, the SEC released the Code, effective January 1, 2017. The Code aims to raise Philippine corporate governance standards to a level that is in line with best practices promulgated in regional and international counterpart markets.

The Code lays out a broad set of guidelines that adopt a “comply or explain” approach where compliance is not mandatory, differentiating from the previous Code’s mandatory/voluntary approach. At this time, the Code does not prescribe a “one size fits all” framework given the widely varying levels of resources available to companies throughout the market. In general, larger corporations are expected to follow the Code’s provisions while smaller companies may decide that certain provisions are less relevant or too costly.<sup>1</sup>

Pursuant to the Code, public companies were required to submit a new Manual on Corporate Governance to the SEC by June 1, 2017 demonstrating which principles they have complied with thus far. In addition, companies also identified areas of noncompliance and included explanations or alternatives to the Code’s provisions.

## SHAREHOLDER MEETINGS AND DISCLOSURE

Pursuant to the Revised Corporation Code, a company’s annual shareholder meeting must be held on the date stated in the Company’s by-laws, or if not stated, on any date after April 15 of every year as determined by the company’s board of directors.

Further, companies are required to send out a written meeting notice and agenda at least 21 days prior to the regular meeting of shareholders and at least one week prior to the special meeting of shareholders.<sup>2</sup>

With regard to disclosure of company information, Philippine companies have generally been characterized as lagging behind their counterparts in other ASEAN countries. However, due to efforts of the SEC and PSE in promoting better corporate governance, information has become steadily available and is expected to further improve with the release of the Code, which will include several recommendations which should improve disclosure and transparency.

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<sup>1</sup> “Code of Corporate Governance for Publicly Listed Companies.” November 22, 2016. Page 4.

<sup>2</sup> Sec. 49, Revised Corporation Code. Recommendation 13.2 of the Code notes that general meeting notices and materials should be made available 28 days ahead of a general meeting.

## **SUMMARY OF CHANGES FOR THE 2020 PHILIPPINES POLICY GUIDELINES**

Glass Lewis evaluates these guidelines on an ongoing basis and formally updates them on an annual basis. This year we've made noteworthy revisions in the following areas, which are summarized below but discussed in greater detail in the relevant sections of this document:

### **CORPORATE GUARANTEES**

We have added our policy for how we will assess the granting of corporate guarantees by companies to other entities.

### **COMMITTEE INDEPENDENCE**

We have updated our approach to voting recommendations on the basis of committee independence for audit, risk, remuneration, nomination, and governance committees.

### **ELECTIONS INVOLVING MORE CANDIDATES THAN SEATS**

We have added our policy for how we may recommend shareholders vote on the election of director proposals when there may be more nominees than seats.

### **PROFESSIONAL SERVICES**

We have updated our policy for evaluating directors who provide professional services.

# A Board of Directors that Serves the Interests of Shareholders

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## CUMULATIVE VOTING

The Revised Corporation Code mandates the use of cumulative voting in the election of directors.<sup>3</sup> Under the cumulative voting system, each shareholder may vote the number of shares held for as many persons as there are directors to be elected, may cumulate said shares and give one nominee all the votes or may distribute them among as many nominees as they so desire, provided that the aggregate number of votes cast shall not exceed the number of shares owned multiplied by the total number of nominees. However, shareholders may be limited to voting only on the entire slate of directors due to common voting procedures in the Philippines.

## ELECTIONS INVOLVING MORE CANDIDATES THAN SEATS

Occasionally among Philippine companies, there may be director elections where there are more candidates than available board seats. At the same time, management generally does not express a recommendation regarding a preferred candidate and shareholders are left to apply their discretion as to which candidate to support. Shareholders are not prevented from supporting all candidates, even if there are more candidates than available board seats.

We believe that at certain companies, particularly those with a dominant controlling shareholder or shareholder group, other shareholders may benefit from more verifiably “outside” representation on the board. In such instances, we will consider recommending to vote for directors who are not affiliated with the major or controlling shareholders, or nominees proposed by minority shareholders where sufficient information regarding the nominee has been disclosed, and where the nominee is appropriately qualified for the role. In cases where multiple minority representative candidates have been nominated, we will base our recommendation on the nominees’ qualifications and experience, and on the company’s shareholder structure.

Moreover, where we have any concerns that an incumbent candidate, whether initially proposed by the company or by a minority shareholder, is not independent or has not demonstrated sufficiently independent judgment in their performance on the board, we will consider supporting a competing candidate providing the criteria above are met.

In evaluating the suitability of competing candidates to the board, we may include a board skills matrix, company disclosure permitting, to aid in assessing the current board’s competencies and identifying any potential skills gaps.

## BOARD OF DIRECTORS

The board structure of Philippine companies, whether listed or otherwise, is best categorized as one-tier. Boards are typically comprised of executive directors and non-executives with only a small independent representation. Many Philippine companies are family-owned or predominantly owned and managed by a small number of shareholder groups and directors are often nominated by the controlling shareholders.

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<sup>3</sup> Sec. 23, Revised Corporation Code.

Glass Lewis looks for talented boards with a record of protecting shareholders and delivering value over the medium- and long-term. We believe that boards working to protect and enhance the best interests of shareholders are independent, have a record of positive performance, and have members with a breadth and depth of experience.

In an effort to facilitate shareholder voting in favor of governance structures that will create shareholder value and maintain a highly functioning independent board, Glass Lewis looks into various aspects of the board and its committee structure and the qualifications of the respective members.

## INDEPENDENCE OF DIRECTORS

The independence of directors, or lack thereof, is ultimately demonstrated through the decisions they make. In assessing the independence of directors, we will take into consideration, when appropriate, whether a director has a track record indicative of making objective decisions. Similarly, instances when a director sits on multiple boards and has a track record that indicates a lack of objective decision making will also be considered when assessing the independence of directors. Ultimately, the determination of whether a director is independent or not must take into consideration both the compliance with the applicable independence listing requirements as well as past conduct.

We look at each director nominee to examine the director's relationships with the company, the company's executives, and other directors. We do this to find personal, familial, or financial relationships (not including director remuneration) that may impact the director's decisions. We believe that such relationships make it difficult for a director to put shareholders' interests above the director's or the related party's interests. We also believe that a director who owns more than 2% of a company can exert disproportionate influence on the board.

Thus, we put directors into three categories based on an examination of the type of relationship they have with the company:

**Independent Director** — A director is independent if he/she has had within the past three years no material,<sup>4</sup> financial, familial<sup>5</sup> or other current relationships with the company,<sup>6</sup> its executives or other board members except for service on the board and standard fees paid for that service. An individual who has been employed by the company, its holding group, or its subsidiaries within the past five years is not considered to be independent.<sup>7</sup>

However, we will not consider a director to be independent if they have progressively been re-designated from an executive director to an independent director despite never leaving the board. We believe that where a director transitions from an executive director to an independent director, they must leave a board for a period of time before rejoining the board with a designation as non-executive or independent director.

**Affiliated Director**<sup>8</sup> — A director is affiliated if he/she has a material, financial, familial or other relationship with the company or its executives, but is not an employee of the company. This includes directors whose employers have a material financial relationship with the Company. This also includes a director

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4 A material relationship is one in which the dollar value exceeds 1% of either company's consolidated gross revenue for other business relationships (e.g., where the director is an executive officer of a company that provides services or products to or receives services or products from the company).

5 "Familial" as used herein includes a person's spouse, parents, children, siblings and the spouse of such sibling or child.

6 "Company" includes any parent or subsidiary in a consolidated group with the company or any entity that merged with, was acquired by, or acquired the company, as well as any companies that are related to the company.

7 The 2015 Implementing Rules has shortened the look-back period for affiliations from five-years to two-years. However, we believe the five-year and three-year time frame is more appropriate. In our view, we believe that two years is not sufficient enough to complete the unwinding of conflicting relationships. If the timing of the cessation of a relationship is not disclosed, as a general rule we will treat the relationship as having existed until recently.

8 In every instance in which a company classifies one of its directors as non-executive, that director will be classified as an affiliate by Glass Lewis.

who owns or controls 2% or more of the company's voting stock.<sup>9</sup>

This classification will also apply to a director who has served as an independent director for more than nine years.<sup>10</sup>

**Inside Director** — An inside director is one who simultaneously serves as a director and as an employee of the company. This category may include a board chair who acts as an employee of the company or is paid as an employee of the company.

### Voting Recommendations on the Basis of Board Independence

Glass Lewis believes that a board will most effectively perform the oversight necessary to protect the interests of shareholders if it is independent. Pursuant to the best practice recommendations under the Code, companies should have a board of directors with a minimum of the higher of: (i) at least three independent directors; or (ii) at least 33% independence of the board.<sup>11</sup> In line with international best practices, we will recommend voting against the necessary number of insiders and/or affiliates to reach this independence standard.

## PERFORMANCE

The most crucial test of a board's commitment to the company and its shareholders lies in the actions of the board and its members. We look at the performance of these individuals in their capacity as directors and executives of the company, as well as their performance in positions at other companies where they have served. We also look at how directors voted while on the board.

### Voting Recommendations on the Basis of Performance

We disfavor directors who have a record of not fulfilling their responsibilities to shareholders at any company where they have held a board or executive position. We typically recommend voting against:

- A director who fails to attend a minimum of 75% of the board meetings or 75% of total applicable committee meetings and board meetings. While we generally recommend directors to attend board meetings in person, we understand it is not always feasible to do so. Therefore, when evaluating a director's attendance, we will consider a director's participation via electronic communication means, such as audio, video or web conferencing devices.<sup>12 13</sup>

Where companies fail to disclose the complete attendance records of the board and its required committees,<sup>14</sup> we will recommend shareholders vote against the board chair. Further, when the attendance record is not disclosed, we will not exempt executives from serving on more than two public company boards.

- A director who is also the CEO of a company where a serious and material restatement has occurred, after the CEO had previously certified the pre-restatement financial statements.

<sup>9</sup> Recommendation 5.2(d), the Code.

<sup>10</sup> Recommendation 5.3, the Code.

<sup>11</sup> Recommendation 5.1, the Code.

<sup>12</sup> However, if a director has served for less than one full year, we will not typically recommend voting against him/her for a failure to attend 75% of meetings. Rather, we will note the failure and track this issue going forward. We will also refrain from voting against directors when the proxy discloses that the director missed the meetings due to serious illness or other extenuating circumstances.

<sup>13</sup> Per Recommendation 4.1 of the Code, where a director is absent in more than 50% of all regular and special board meetings during their incumbency or during a 12-month period, they will be disqualified as a director, unless the absence is due to illness, death in the immediate family or serious accident. The disqualification will apply for purposes of the succeeding election.

<sup>14</sup> The required committees will primarily be the audit, corporate governance, and/or nomination, and remuneration committees.



- All members of the board if a company's performance has been consistently lower than its peers and the board has not taken reasonable steps to address the poor performance.

## EXPERIENCE

We find that a director's past conduct is often indicative of future conduct and performance. We often find directors with a history of overcompensating executives or with a history of serving on boards where significant and avoidable disasters have occurred, reappearing at companies that follow these same patterns.

### **Voting Recommendations on the Basis of Director Experience**

We believe that boards should have diverse backgrounds and members with a breadth and depth of relevant experience. We believe that the nomination committee should consider diversity when making director nominations within the context of each specific company and its industry. In our view, shareholders are best served when boards make an effort to ensure a constituency that is not only reasonably diverse on the basis of age, race, gender and ethnicity, but also on the basis of geographic knowledge, industry experience, board tenure and culture.

We typically recommend that shareholders vote against directors who have served on boards or as executives of companies with a track record of poor performance, over-remuneration, audit or accounting related issues and/or other indicators of mismanagement or actions against the interests of shareholders.

Similarly, we examine the backgrounds of those who serve on key board committees to ensure that they have the required skills and diverse backgrounds to make informed judgments about the subject matter for which the committee is responsible.

## INDEPENDENT DIRECTOR BOARD TENURE

Under SEC rules, after nine years of cumulative service on a board, a director will cease to be considered as independent. Where we find that an independent director has served for more than nine years on a cumulative basis as of the upcoming general meeting, we will re-classify that independent director as being a non-independent non-executive director.<sup>15</sup>

## DIRECTOR COMMITMENTS

We believe that directors should have the necessary time to fulfill their duties to shareholders. In our view, an overcommitted director can pose a material risk to a company's shareholders, particularly during periods of crisis. We believe this limits the number of boards on which directors and statutory auditors can effectively serve, especially executives at other companies.

### **Voting Recommendations on the Basis of Director Commitments**

We will generally recommend that shareholders vote against a director who serves as an executive officer of any public company while serving on more than two public company boards and any other director who serves on more than five public company boards. We will also count individuals who serve as board chair of boards in select other non-Asian markets, per our global policies, as two board seats given the time commitment of directorship in those markets.

Because we believe that executives will primarily devote their attention to executive duties, we generally will

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<sup>15</sup> Recommendation 5.3, the Code.

not recommend that shareholders vote against overcommitted directors at the companies where they serve as an executive. Provided board attendance records are disclosed and directors attended 75% of the board and committee meetings.

When determining whether a director's service on an excessive number of boards may limit the ability of the director to devote sufficient time to board duties, we may consider relevant factors such as the size and location of the other companies where the director serves on the board, the director's board roles at the companies in question, whether the director serves on the board of any large privately-held companies, the director's tenure on the boards in question, and the director's attendance record at all companies.

We may also refrain from recommending against certain directors if the company provides sufficient rationale for their continued board service. The rationale should allow shareholders to evaluate the scope of the directors' other commitments as well as their contributions to the board, including specialized knowledge of the company's industry, strategy or key markets, the diversity of skills, perspective and background they provide, and other relevant factors.

## CONFLICT OF INTEREST

In addition to the key characteristics — performance, director commitments and performance — that we use to evaluate board members, we consider the following issues in making voting recommendations.

Irrespective of the overall presence of independent directors on the board, we believe that a board should be wholly free of people who have an identifiable and substantial conflict of interest. Accordingly, we recommend shareholders vote against the following types of directors under nearly all circumstances:

### Voting Recommendations on the Conflict of Interest

- **Professional Services and Business Transactions** — A director or a director who has an immediate family member, providing material professional services during the last fiscal year or on an ongoing basis. Material professional services may include legal, consulting or financial services to the company. Also a director who engages — or has a family member of whom engages — in business contracts with the company such as purchase or sales agreement will have to make unnecessarily complicated decisions that may pit their interests against those of the shareholders they serve.<sup>16</sup>
- **Interlocking Directorship** — CEOs or other top executives who serve on each other's boards create an interlock that poses conflicts that should be avoided to ensure the promotion of shareholder interests above all else.<sup>17</sup>

## BOARD SIZE

While we do not believe that there is a universally applicable optimum board size, we do believe that boards should have a minimum of five directors in order to ensure that there is a sufficient diversity of views and breadth of experience in every decision the board makes. At the other end of the spectrum, we believe that an excessive board size will typically suffer under the weight of "too many cooks in the kitchen" and have difficulty reaching consensus and making timely decisions. Sometimes the presence of too many voices makes it difficult to draw on the wisdom and experience in the room by virtue of the need to limit the discussion so that each voice may be heard.

To that end, we typically recommend voting against the nomination committee chair if a board has more than

<sup>16</sup> Recommendation 5.2, paragraphs j, i and j, all generally prohibit the provision of professional services to companies by independent directors. We believe that such limitations should be extended to all directors.

<sup>17</sup> There is no look-back period for this situation. This only applies to public companies and we will only recommend voting against the non-insider executive director.

15 directors. Moreover, while we prefer a minimum board size of five directors, we will not recommend against the chair of the corporate governance or nomination committee, but instead will note our preference for a larger board size.<sup>18 19</sup>

## SEPARATION OF THE ROLES OF BOARD CHAIR AND CEO

Glass Lewis believes that separating the roles of corporate officer and chair creates a better governance structure than a combined executive/chair position. An executive manages the business according to a course the board charts. Executives should report to the board regarding their performance in achieving the board's goals.

This process is needlessly complicated when a CEO sits on or chairs the board, since a CEO presumably will have significant influence over the board. It can become difficult for a board to fulfill its role of overseer and policy-setter when a CEO/chair controls the agenda and the boardroom discussion. Such control can allow a CEO to have an entrenched position, leading to longer-than-optimal terms, fewer checks on management, less scrutiny of the business operation and limitations on independent, shareholder-focused goal-setting by the board.

A CEO should set the strategic course for the company, with the board's approval, and the board should enable the CEO to carry out his/her vision for accomplishing the board's objectives. The failure to achieve the board's objectives should lead it to replace the CEO with someone in whom it has more confidence.

Similarly, an independent chair can better oversee executives and set a pro-shareholder agenda without the management conflicts that a CEO or other executive insider often faces. Such oversight and concern for shareholders allows for a more proactive and effective board of directors that is better able to look out for the interests of shareholders.

We do not recommend that shareholders vote against CEOs who serve on or chair the board. However, we typically encourage our clients to support separating the roles of chair and CEO whenever that question is posed in a proxy (typically in the form of a shareholder proposal), as we believe that it is in the long-term best interests of the company and its shareholders.

The Code recommends that the roles of chair and CEO be separated.<sup>20</sup> It is also recommended that if the roles are not separated, companies should emplace proper mechanisms to prevent conflict such as the appointment of a leading independent director. In line with best practices, we will recommend voting against the nominating committee chair when the company asks shareholder to appoint a director as chair and CEO and there is no independent vice chair or leading/senior independent director on the board.

## DISCLOSURE OF ANNUAL REPORT AND INFORMATION STATEMENTS

We believe that public companies have a responsibility to disclose information to shareholders in a timely and transparent manner. We are concerned that a short timeframe to review proxy materials prevents shareholders from making informed decisions. Therefore, we strongly encourage companies to disclose annual reports and information statements well in advance of annual meetings to allow for meaningful review. To this end, when a company fails to release the annual report or Definitive Information Statement at least 14 days before an annual general meeting,<sup>21</sup> we will recommend voting against the board chair for failing to disclose relevant information. In case an annual report or Definitive Information Statement for the most recently completed fiscal year is unavailable, we will base our analysis on secondary company filings as well as information disclosed on

<sup>18</sup> The SEC stipulates that a board should be composed of at least five but not more than 15 directors.

<sup>19</sup> In the absence of a nomination committee, we will recommend voting against the board chair.

<sup>20</sup> Recommendation 5.4, the Code.

<sup>21</sup> We will apply local time.

the PSE Electronic Disclosure Generation Technology (“PSE EDGE”) and company websites.<sup>22</sup>

## BOARD EVALUATION AND REFRESHMENT

Glass Lewis strongly supports routine director evaluation, including independent external reviews, and periodic board refreshment to foster the sharing of diverse perspectives in the boardroom and the generation of new ideas and business strategies. Further, we believe the board should evaluate the need for changes to board composition based on an analysis of skills and experience necessary for the company, as well as the results of the director evaluations, as opposed to relying solely on age or tenure limits. When necessary, shareholders can address concerns regarding proper board composition through director elections.

In our view, a director’s experience can be a valuable asset to shareholders because of the complex, critical issues that boards face. This said, we recognize that in rare circumstances, a lack of refreshment can contribute to a lack of board responsiveness to poor company performance.

On occasion, age or term limits can be used as a means to remove a director for boards that are unwilling to police their membership and enforce turnover. Some shareholders support term limits as a way to force change in such circumstances.

While we understand that age limits can aid board succession planning, the long-term impact of age limits restricts experienced and potentially valuable board members from service through an arbitrary means. We believe that shareholders are better off monitoring the board’s overall composition, including its diversity of skill sets, the alignment of the board’s areas of expertise with a company’s strategy, the board’s approach to corporate governance, and its stewardship of company performance, rather than imposing inflexible rules that don’t necessarily correlate with returns or benefits for shareholders.

However, if a board adopts term/age limits, it should follow through and not waive such limits. If the board waives its term/age limits, Glass Lewis will consider recommending shareholders vote against the nominating and/or governance committees, unless the rule was waived with sufficient explanation, such as consummation of a corporate transaction like a merger.

## BOARD GENDER DIVERSITY

Glass Lewis recognizes the importance of ensuring that the board is comprised of directors who have a diversity of skills, thought and experience, as such diversity benefits companies by providing a broad range of perspectives and insights.<sup>23</sup>

As the Code recommends that companies explore gender diversity,<sup>24</sup> such as by increasing the number of independent women on the board, we believe that all companies must have at least one female director. Glass Lewis will generally recommend voting against the nomination committee chair where boards do not have at least one female director. Depending on other factors, including the size of the company, the industry in which the company operates and the governance profile of the company, we may extend this recommendation to vote against other nominating committee members. When making these voting recommendations, we will carefully review a company’s disclosure of its diversity considerations and may refrain from recommending shareholders vote against directors of companies when boards have provided a sufficient rationale for not having any female board members. Such rationale may include, but is not limited to, a disclosed timetable for addressing the lack of diversity on the board, and any notable restrictions in place regarding the board’s composition, such as director nomination agreements with significant investors.

<sup>22</sup> The 2015 Blueprint states that companies must disclose 14 days prior to the meeting, however, Recommendation 13.2 of the Code states that companies should disclose at least 28 days before the meeting in order to encourage shareholder participation. Yet, Section 49 of the Revised Corporation Code provides for meeting notice periods being 21 days before general meetings.

<sup>23</sup> See our In Depth Report on Gender Diversity, available at [www.glasslewis.com/special-reports/](http://www.glasslewis.com/special-reports/).

<sup>24</sup> Recommendation 1.4, the Code.

## INITIAL PUBLIC OFFERING

Where a company recently completed its initial public offering (“IPO”) and became listed on the stock exchange, we will exempt the company from our guidelines for a period of the first financial year or 12 months from the IPO date, whichever is longer.

However, we will review our exemption on a case-by-case basis if: (i) a company and/or its board members are the subject of serious regulatory investigations or actions; and/or (ii) there are significant concerns about overall corporate governance practices.

## BOARD COMMITTEES

In accordance with the relevant laws and regulations, every listed company shall have an audit committee. The audit committee must comprise a minimum of three directors, comprising a majority of independent directors, while the audit committee chair should be an independent director.<sup>25</sup> The audit committee should have one member who has accounting or related financial management expertise. In addition, we will recommend voting against any member of the audit committee who owns 20% or more of the company’s stock.

The Code recommends that companies establish a corporate governance committee or separate nomination and remuneration committees, each consisting of at least three directors. While the Code recommends that both nomination and remuneration committees to be solely independent, we believe that these committees should comprise majority independent directors.<sup>26</sup> In addition, we believe that remuneration committee which is responsible for determining the remuneration of executives and directors should be chaired by an independent director. In the case that the company has not established a nomination or remuneration committee, we will recommend voting against the board chair.

Although the Code notes that committee functions may be carried out by the whole board or any other committees,<sup>27</sup> Glass Lewis expects all companies to have distinct committees. In the absence of such committees, Glass Lewis will expect an explanation for how one committee would fulfil these multiple functions. In the absence of distinct board committees or a reasonable explanation, we will recommend shareholders vote against the board chair.

Furthermore, we typically recommend that shareholders vote against any insider or affiliated director seeking appointment to an audit, remuneration or nomination committee when the committees do not meet the independence standards, which we believe are appropriate.

## AUDIT COMMITTEE PERFORMANCE

Audit committees play an integral role in overseeing the financial reporting process because “vibrant and stable capital markets depend on, among other things, reliable, transparent, and objective financial information to support an efficient and effective capital market process. The vital oversight role audit committees play in the process of producing financial information has never been more important.”<sup>28</sup>

When assessing an audit committee’s performance, we are aware that an audit committee does not prepare financial statements, is not responsible for making the key judgments and assumptions that affect the financial statements, and does not audit the numbers or the disclosures provided to investors. Rather, an audit committee member monitors and oversees the process and procedures that management and auditors perform. The 1999 Report and Recommendations of the Blue Ribbon Committee on Improving the Effectiveness of Corporate

<sup>25</sup> Recommendation 3.2, the Code.

<sup>26</sup> Recommendation 3.3, the Code.

<sup>27</sup> Recommendation 3.1, the Code.

<sup>28</sup> “Audit Committee Effectiveness – What Works Best.” PricewaterhouseCoopers. The Institute of Internal Auditors Research Foundation. 2005.

Audit Committees stated it best:

*A proper and well-functioning system exists, therefore, when the three main groups responsible for financial reporting — the full board including the audit committee, financial management including the internal auditors, and the outside auditors — form a ‘three legged stool’ that supports responsible financial disclosure and active participatory oversight. However, in the view of the Committee, the audit committee must be ‘first among equals’ in this process, since the audit committee is an extension of the full board and hence the ultimate monitor of the process.*

For an audit committee to function effectively on investors’ behalf, it must include members with sufficient knowledge to diligently carry out their responsibilities. In its audit and accounting recommendations, the Conference Board Commission on Public Trust and Private Enterprise said “members of the audit committee must be independent and have both knowledge and experience in auditing financial matters.”<sup>29</sup>

We are skeptical of audit committees where there are members that lack expertise in finance and accounting or in any other equivalent or similar areas of expertise. While we will not necessarily vote against members of an audit committee when such expertise is lacking, we are more likely to vote against committee members when a problem such as a restatement occurs and such expertise is lacking.

Glass Lewis generally assesses audit committees taking the decisions they make with respect to their oversight and monitoring role into consideration. The quality and integrity of the financial statements and earnings reports, the completeness of disclosures necessary for investors to make informed decisions, and the effectiveness of the internal controls should provide reasonable assurance that the financial statements are materially free from errors. The independence of the external auditors and the results of their work all provide useful information by which to assess the audit committee.

When assessing the decisions and actions of the audit committee, we typically defer to its judgment and would vote in favor of its members, but we would recommend voting against the following members under the following circumstances:<sup>30</sup>

- The audit committee chair if the committee is chaired by a non-independent director.
- Any audit committee member who is considered an executive or employee of the company based on our research.
- Any audit committee member who is not considered independent, when the committee is not majority independent.
- Any member of the audit committee who owns or represents an entity that owns 20% or more of the company’s stock.
- The audit committee chair when fees for non-audit services are greater than audit and audit-related fees paid to the auditor for one financial year.
- All serving members of an audit committee, when fees for non-audit services are greater than audit and audit-related fees paid to the auditor for two or more consecutive financial years.

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<sup>29</sup> Commission on Public Trust and Private Enterprise. The Conference Board. 2003.

<sup>30</sup> If our recommendation is to vote against the committee chair and the chair of the committee is not specified, we will recommend voting against the director who has been on the committee the longest as the de facto chair.

- All members of an audit committee where non-audit fees include fees for tax services for senior executives of the company or involve services related to tax avoidance or tax shelter schemes.
- All members of an audit committee that re-appointed an auditor that we no longer consider to be independent for reasons unrelated to fee proportions.
- The audit committee chair where there is no proposal at the AGM to ratify the appointment of a company's auditor.
- All members of an audit committee at a time when accounting fraud occurred in the company.
- All members of an audit committee at a time when financial statements had to be restated due to negligence or fraud.
- All members of an audit committee if the company repeatedly fails to file its financial reports in a timely fashion.
- All members of an audit committee at a time when the company fails to report or to have its auditors report material weaknesses in internal controls.
- The audit committee chair if the committee does not have at least one member with "appropriate accounting or related financial management expertise."
- The audit committee chair if the committee has fewer than three members.
- The audit committee chair if the company failed to disclose the fees paid to the auditor including the breakdown thereof.
- The audit committee chair if non-board members serve on the audit committee.<sup>31</sup>
- The audit committee chair if the audit committee did not meet at least four times during the year.
- The board chair if the company has not established an audit committee.

We also take a critical view of audit committee reports that are boilerplate, and which provide little or no information or transparency to investors. When a problem such as a material weakness, restatement or late filings occurs, we take it into consideration, in forming our judgment with respect to the audit committee, and the transparency of the audit committee report.

## CORPORATE GOVERNANCE COMMITTEE

The Code recommends that companies establish a new corporate governance committee to assist the board. The responsibilities and functions of the committee were previously assigned to the nomination and/or remuneration committees. For companies who adhere to this principle of adopting a corporate governance committee instead of separate nomination and remuneration committees, we will evaluate this committee as if it were a combined nomination and remuneration committee. Below are Glass Lewis' general guidelines on

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<sup>31</sup> Regardless of whether or not the non-board member is a voting or non-voting member, we do not believe it is in the best interest of shareholders to support a committee structure which allows for members who have not been elected by shareholders to serve on a committee. We believe the committee should be in a position to invite non-members to their committee meetings when necessary.

how remuneration and nomination committees should perform.<sup>32</sup>

## REMUNERATION COMMITTEE PERFORMANCE

Remuneration committees have the final say in determining the remuneration of executives. This includes deciding the basis on which remuneration is determined, as well as the amounts and types of remuneration to be paid. This process begins with the hiring and initial establishment of employment agreements, including the terms for such items as pay, pensions and severance arrangements. It is important in establishing remuneration arrangements that remuneration be consistent with, and based on, the long-term economic performance of the business's long-term shareholder returns.

Remuneration committees are also responsible for the oversight of the transparency of remuneration. This oversight includes disclosure of remuneration arrangements, the matrix used in assessing pay for performance, and the use of remuneration consultants. It is important to investors that they have clear and complete disclosure of all the significant terms of remuneration arrangements in order to make informed decisions with respect to the oversight and decisions of the remuneration committee.

Finally, remuneration committees are responsible for oversight of internal controls over the executive remuneration process. This includes controls over gathering information used to determine remuneration, establishment of equity award plans, and granting of equity awards. Lax controls can and have contributed to conflicting information being obtained, for example through the use of nonobjective consultants. Lax controls can also contribute to improper awards of remuneration such as through granting of backdated or spring-loaded options, or granting of bonuses when triggers for bonus payments have not been met.

We evaluate remuneration committee members on the basis of their performance while serving on the remuneration committee in question, not for actions taken solely by prior committee members who are not currently serving on the committee.

When assessing the performance of remuneration committees, we will recommend voting against the following:<sup>33</sup>

- The remuneration committee chair if the committee is chaired by a non-independent director.
- Any remuneration committee member who is considered an executive or employee of the company based on our research.
- Any remuneration committee member who is not considered independent, when the committee is not majority independent.
- All members of the remuneration committee (from the relevant time period) if excessive employment agreements and/or severance agreements were entered into.
- All members of the remuneration committee if performance goals were changed (i.e., lowered) when employees failed or were unlikely to meet original goals or performance-based remuneration was paid despite goals not being attained.
- All members of the remuneration committee if excessive employee perquisites and benefits were allowed.

<sup>32</sup> Recommendation 3.3 of the Code states that companies should adopt a corporate governance committee.

<sup>33</sup> If our recommendation is to vote against the committee chair and the chair of the committee is not specified, we will recommend voting against the director who has been on the committee the longest as the de facto chair.



- The remuneration committee chair if the remuneration committee did not meet during the year, but should have (e.g., executive remuneration was restructured).
- The remuneration committee chair if non-board members serve on the remuneration committee.<sup>34</sup>
- The remuneration committee chair if the committee has fewer than three members.
- The board chair if the company has not established a remuneration committee.

## NOMINATION COMMITTEE PERFORMANCE

The nomination committee, as an agency for the shareholders, is responsible and accountable for selection of objective and competent board members.

Regarding the nomination committee, we will recommend voting against the following:<sup>35</sup>

- The nomination committee chair if the committee is chaired by a non-independent director.
- Any nomination committee member who is not considered independent, when the committee is not majority independent.
- All members of the nomination committee when the committee nominated or re-nominated an individual who had a significant conflict of interest or who's past actions demonstrated a lack of integrity or inability to represent shareholder interests.
- Any committee member who is considered an executive or employee of the company based on our research, when the committee is combined with a remuneration committee.
- The nomination committee chair if: (i) the nomination committee did not meet during the year, but should have (i.e., new directors were nominated); (ii) the committee re-nominated a director who did not attend any board meetings; or (iii) the committee re-nominated a director who attended less than 75% of the meetings held by the board and/or the committees for two or more consecutive years.
- The nomination committee chair if: (i) at least three directors or 33% of the board, whichever is higher, is not independent; or (ii) there are more than 15 members on the board.
- The nomination committee chair where the board does not have at least one female director.
- The nomination committee chair if non-board members serve on the committee.<sup>36</sup>
- The nomination committee chair if the committee has fewer than three members.
- The board chair if the company has not established a nomination committee.

<sup>34</sup> Regardless of whether or not the non-board member is a voting or non-voting member, we do not believe it is in the best interest of shareholders to support a committee structure that allows for members who have not been elected by shareholders to serve on a committee. We believe the committee should be in a position to invite non-members to their committee meetings when necessary.

<sup>35</sup> If our recommendation is to vote against the committee chair and the chair of the committee is not specified, we will recommend voting against the director who has been on the committee the longest as the de facto chair.

<sup>36</sup> Regardless of whether or not the non-board member is a voting or non-voting member, we do not believe it is in the best interest of shareholders to support a committee structure which allows for members who have not been elected by shareholders to serve on a committee. We believe the committee should be in a position to invite non-member to their committee meetings when necessary..

- The nomination committee chair if the chair of the board is a part of the management team and there is no independent vice chair or leading/senior independent director on the board.<sup>37</sup>

## RISK OVERSIGHT COMMITTEE PERFORMANCE

The Code recommends that conglomerates and companies with a high risk profile should establish a risk oversight committee.<sup>38</sup> This committee, if separate from the audit committee, would be responsible for ensuring robust internal control systems to oversee and manage a company's risk profile.

Where a company has a risk committee, we will expect the committee to be chaired by an independent non-executive director. We will recommend against any risk committee member who is considered an executive or employee of the company based on our research, along with any risk committee member who is not considered independent, when the committee is not majority independent.<sup>39</sup> Where companies establish a risk committee, we will count the attendance of directors serving on this committee, along with attendance for board and other committee meetings.

Where a company establishes this type committee, we will recommend against members of this committee in instances or events where there has been a failure of risk management.

## ENVIRONMENTAL AND SOCIAL RISK OVERSIGHT

Glass Lewis understands the importance of ensuring the sustainability of companies' operations and believes that an inattention to material environmental and social issues can present direct legal, financial, regulatory and reputational risks for companies that could serve to harm shareholder interests. Therefore, we believe that these issues should be carefully monitored and managed by companies and that companies should have an appropriate oversight structure in place to ensure that they are mitigating attendant risks and capitalizing on related opportunities to the best extent possible.

Glass Lewis believes that companies should ensure appropriate, board-level oversight of material risks to their operations, including those that are environmental and social in nature. Accordingly, in instances where we identify material oversight issues, Glass Lewis will review a company's overall governance practices and identify which directors or board-level committees have been charged with oversight of environmental and/or social issues.

Where it is clear that companies have not properly managed or mitigated environmental or social risks to the detriment of shareholder value or when such mismanagement has threatened shareholder value, Glass Lewis may consider recommending that shareholders vote against members of the board who are responsible with oversight of environmental and social risks. In the absence of explicit board oversight of environmental and social issues, Glass Lewis may recommend that shareholders vote against members of the audit committee, risk committee or other applicable committees. In making these determinations, Glass Lewis will carefully review the situation at hand, its effect on shareholder value, as well as any corrective action or other response made by the company.

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<sup>37</sup> Recommendation 5.5, the Code.

<sup>38</sup> Recommendation 3.4, the Code.

<sup>39</sup> Recommendation 3.4, the Code.

# Transparency and Integrity in Financial Reporting

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## ACCOUNTS AND REPORTS

In the Philippines, companies are required to submit annual financial statements<sup>40</sup> and other relevant reports to be approved by shareholders for them to be legally valid. We will recommend voting for these proposals except in the case where there are concerns about the integrity of the statements/reports. Should an auditor be unable to ensure a clean bill of health, depending on the circumstance, we may recommend that shareholders abstain from voting or vote against the auditor in addition to recommending voting against members of the audit committee.

However, in the event that the audited financial statements have not been made available, we do not believe shareholders have sufficient information to make an informed judgment regarding this matter. In those cases, we will recommend that shareholders abstain from voting on this agenda item.

## ALLOCATION OF PROFITS/DIVIDENDS

Glass Lewis generally supports a company's policy when it comes to the payment of dividends including decisions not to pay them. In most cases, we believe the board is in the best position to determine whether a company has sufficient resources to distribute a dividend or if shareholders would be better served by forgoing a dividend to conserve resources for future opportunities or needs. As such, we will only recommend that shareholders refrain from supporting dividend proposals in exceptional cases.

## APPOINTMENT/RATIFICATION OF AUDITOR

The auditor's role as gatekeeper is crucial in ensuring the integrity and transparency of the financial information necessary for protecting shareholder value. Shareholders rely on the auditor to ask tough questions and to do a thorough analysis of a company's books to ensure that the information provided to shareholders is complete, accurate, fair, and that it is a reasonable representation of a company's financial position. The only way shareholders can make rational investment decisions is if the market is equipped with accurate information about a company's fiscal health.

Shareholders should demand an objective, competent and diligent auditor who performs at or above professional standards at every company in which the investors hold an interest. Like directors, auditors should be free from conflicts of interest and should avoid situations requiring a choice between the auditor's interests and the public's interests. Almost without exception, shareholders should be able to annually review an auditor's performance and to annually ratify a board's auditor selection.

When ratification of the auditor is submitted to shareholders for their approval, we generally support management's choice of auditor except when we believe the auditor's independence or audit integrity has been

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<sup>40</sup> Including income statements, balance statements and any relevant notes.

compromised.<sup>41</sup> When there have been material restatements of annual financial statements or material weakness in internal controls, we usually recommend voting against the auditor. In the event that the audited financial statements have not yet been disclosed, we base our voting recommendations on the company's financial statements for the previous year. We do not hold a company's auditor responsible for, what we believe, may be the company's failure to comply with reporting obligations or a lack thereof, depending on the jurisdiction.

Reasons why we may not recommend ratification of an auditor include:

- Where the company failed to disclose the auditor fees paid for the previous fiscal year or a breakdown thereof.
- When audit and audit-related fees total 50% or less of the overall fees billed by the auditor.
- Recent material restatements of annual financial statements have been made, including those resulting in the reporting of material weaknesses in internal controls and including late filings by the company where the auditor bears some responsibility for the restatement or late filing.<sup>42</sup>
- When the company has aggressive accounting policies evidenced by restatements or other financial reporting problems.
- When the company has poor disclosure or lack of transparency in its financial statements.
- When the auditor has limited its liability through its contract with the company.
- When other relationships or concerns with the auditor suggest a conflict between the auditor's interests and shareholder interests.
- In cases where the company does not disclose sufficient information regarding the appointment or ratification of the auditor (e.g., the name of the auditor), we will recommend an abstain vote.

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<sup>41</sup> If ratification of the auditor is not presented to shareholders for their approval and if we find a significant concern with the auditor, we may recommend shareholders vote against the election of audit committee members.

<sup>42</sup> An auditor does not audit interim financial statements. Thus, we generally do not believe that an auditor should be opposed due to a restatement of interim financial statements, unless the nature of the misstatement is clear from a reading of the incorrect financial statements.

# The Link Between Compensation and Performance

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## DIRECTOR REMUNERATION

Glass Lewis believes that directors should receive remuneration for the time and effort they spend serving on the board and its committees. In particular, we support remuneration plans that include option grants or other equity-based awards that help to align the interests of outside directors with those of shareholders. Director fees should be competitive in order to retain and attract qualified individuals. But excessive fees represent a financial cost to the company and threaten to compromise the objectivity and independence of non-employee directors. Therefore, a balance is required.

Pursuant to the Revised Corporation Code, directors are not allowed to receive any compensation except for reasonable per diems unless specific provisions are included in the company's by-laws and must be approved by shareholders.<sup>43</sup> Therefore, while shareholders are unable to vote on director remuneration on an annual basis, companies must seek shareholder approval when amending the remuneration policy or structure for its directors.

Glass Lewis generally supports this type of proposal, unless we find the proposed fees are excessive relative to those paid by peer companies with similar market capitalizations or may impair the objectivity and independent of the independent non-executive directors.

## RETIREMENT BENEFITS FOR DIRECTORS

We will typically recommend voting against proposals to grant retirement benefits to non-executive directors. Such extended payments can impair the objectivity and independence of these board members. Directors should receive adequate remuneration for their board service through initial and annual fees.

## EQUITY-BASED COMPENSATION PLANS

We believe that equity compensation awards are useful, when not abused, for retaining employees and providing them with an incentive to act in a way that will improve company performance.

Equity-based compensation programs have important differences from cash compensation plans and bonus programs. Accordingly, our analysis takes into account factors such as plan administration, the method and terms of exercise, and express or implied rights to re-price.

Our analysis is both quantitative and qualitative. In particular, we examine the potential dilution to shareholders, the company's grant history and compliance with best practice recommendations.

We evaluate equity-based compensation plans based on the following overarching principles:

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<sup>43</sup> Sec. 29, Revised Corporation Code.

- Companies should seek more shares only when they need them.
- Plan limits should be small enough that companies need to seek shareholder re-approval at least every three to four years (or less).
- Plans should not permit re-pricing of stock options.
- Plans should not contain excessively liberal administrative or payment terms.

In addition, as a general rule, we do not support granting performance-linked compensation to those who carry out supervisory duties because we believe that a non-executive director should hold the same type of securities as ordinary shareholders. Thus, we recommend shareholders vote against when non-executive directors are eligible to participate in performance-linked plan.

When evaluating equity-based compensation proposals, we will look for companies to provide complete disclosure surrounding the proposed equity grants. In the absence of complete disclosure, we may recommend shareholders oppose either the adoption of an equity-based compensation plan or the granting of equity awards. However, in recognition of equity compensation practices for Philippine companies, we will generally evaluate the general authority to grant awards under equity compensation plans in the following manner:

- For proposals seeking to grant awards within the general limits of an existing plan or plans, if the proposed grant size is not disclosed we will look at the previous year's grants to infer a potential grant size in the current financial year. We will generally recommend shareholders oppose proposals to grant additional equity awards if grants exceeded 2% of a company's issued share capital as at the holding of the general meeting.
- Where companies had existing plans and are looking to adopt a new plan, we will examine whether companies in the preceding two years had plans which granted more than 2% of a company's issued share capital on an annual basis. Where such grant histories are found, we will oppose the adoption of a new equity compensation plan, unless the proposed new plan commits to granting less than 2% of issued share capital on an annual basis.
- Where companies previously did not have equity-compensation plans but are adopting a plan for the first time, we will generally base our recommendation on the qualitative elements of the proposed plan to guide our recommendation, unless the annual grants exceed 2% of a company's issued share capital.

## OPTION EXCHANGES

Glass Lewis views option re-pricing plans and option exchange programs with great skepticism. Shareholders have substantial, real downside risk in owning stock, and we believe that the employees, officers and directors who receive options should be similarly situated to align interests optimally. We are concerned that option grantees who believe they will be "rescued" from underwater options will be more inclined to take on unjustifiable risks. Moreover, a predictable pattern of re-pricing or exchanges substantially alters the value of the stock option, as options that will practically never expire deeply out of the money are worth far more than options that carry such a risk. In short, repricings and option exchange programs change the bargain between shareholders and employees after the bargain has been struck. Re-pricing is tantamount to a re-trade.

There is one circumstance in which a repricing or option exchange program is acceptable: if the value of a stock has declined dramatically because of macroeconomic or industry trends (rather than specific company issues) and a re-pricing is necessary to motivate and retain employees. In this circumstance, we think it fair to

conclude that option grantees may be suffering from a risk that was not foreseeable when the original equity-based compensation “bargain” was struck. In such a circumstance, we will support a re-pricing only if the following conditions are true:

- Officers and board members do not participate in the program.
- The stock decline mirrors the market or industry price decline in terms of timing and approximates the decline in magnitude.
- The exchange is value-neutral or value-creative to shareholders with very conservative assumptions and a recognition of the adverse selection problems inherent in voluntary programs.
- Management and the board make a cogent case for needing to incentivize and retain existing employees, such as the company’s position in a competitive employment market.

## PERFORMANCE-BASED OPTIONS

Shareholders commonly ask boards to adopt policies requiring that a significant portion of future stock option grants to senior executives be based on performance metrics such as performance-based options that have an exercise price linked to an industry peer group’s stock-performance index.

Glass Lewis believes in performance-based equity remuneration plans for senior executives. We feel that executives should be compensated with equity when their performance and that of the Company warrants such rewards.

While we do not believe that equity-based pay plans for all employees should be based on overall company performance, we do support such limitations for equity grants to senior executives. However, some level of equity-based compensation for senior executives without performance criteria is acceptable, such as in the case of moderate incentive grants made in an initial offer of employment or in emerging industries.

Boards often maintain that basing option grants on performance would hinder their ability to attract talent. We believe that boards can develop a consistent, reliable approach to attract executives who are able to guide the company toward its targets. If the board believes in performance-based pay for executives, then these proposals requiring the same should not hamper the board’s ability to create equity-based compensation plans.

We generally recommend that shareholders vote in favor of performance-based option requirements.

## EXECUTIVE COMPENSATION

As a general rule, Glass Lewis believes that shareholders should not be involved in setting executive compensation. Such matters should be left to the board’s remuneration committee. We view the election of directors — specifically, the election of those who sit on the remuneration committee — as the appropriate mechanism for shareholders to express their disapproval or support of board policy on this issue. Further, we believe that companies whose pay-for-performance policies are in line with their peers should be granted the flexibility to compensate their executives in a manner that drives growth and profit.

However, Glass Lewis favors performance-based compensation as an effective means of motivating executives to act in the best interests of shareholders. Performance-based compensation may be limited if a chief executive’s pay is capped at a low level rather than flexibly tied to the performance of the company.

# Governance, Financial Structure and the Shareholder Franchise

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## AMENDMENTS TO THE ARTICLES OF ASSOCIATION

We will evaluate proposed amendments to a company's articles of association on a case-by-case basis. We are opposed to the practice of bundling several amendments under a single proposal because it might force shareholders to vote in favor of amendments that they might otherwise reject had they been submitted as separate proposals. In such cases, we will analyze each change on their own. We will recommend voting for the proposal only when, on balance, we believe that all of the amendments are in the best interests of shareholders.

## DIVIDEND REINVESTMENT (OR SCRIP DIVIDEND) PLAN

We support plans that provide shareholders with the choice of receiving dividends in stock instead of cash. For the company, a stock dividend typically offers a tax benefit. In addition, the company can keep more of its earnings rather than distributing them. For shareholders, a dividend reinvestment plan offers a less expensive way to acquire additional shares. They avoid paying brokers' commissions or the taxes on normal stock transactions. The stock price is usually equal to an average, middle-market price, which is often lower than the price available on the stock exchange.

## INCREASES IN CAPITAL

Glass Lewis believes that adequate capital stock is important to a company's operation. Philippine companies are authorized to increase share capital through several methods, which may or may not involve the issuance of shares.

## ISSUANCE OF SHARES AND/OR CONVERTIBLE SECURITIES

In general, issuing an excessive amount of additional shares and/or convertible securities can dilute existing holders. Further, the availability of additional shares, where the board has discretion to implement a poison pill, can often serve as a deterrent to interested suitors. Accordingly, where we find that the company has not detailed a plan for use of the proposed shares, or where the number of shares far exceeds those needed to accomplish a detailed plan, we typically recommend against the authorization of additional shares.

While we think that having adequate shares to allow management to make quick decisions and effectively operate the business is critical, we prefer that, for significant transactions, management come to shareholders to justify their use of additional shares rather than providing a blank check in the form of a large pool of unallocated shares available for any purpose.

In our view, unless a board provides any compelling reason, in general any authorization to issue shares and/or convertible securities without preemptive rights should not exceed 20% of the company's total share capital. Likewise, we believe the discount rate for the new issue should not exceed 15% of the average market price.



## DUAL-CLASS SHARE STRUCTURES

Glass Lewis believes dual-class voting structures are typically not in the best interests of common shareholders. Allowing one vote per share generally operates as a safeguard for common shareholders by ensuring that those who hold a significant minority of shares are able to weigh in on issues set forth by the board.

Furthermore, we believe that the economic stake of each shareholder should match their voting power and that no small group of shareholders, family or otherwise, should have voting rights different from those of other shareholders. On matters of governance and shareholder rights, we believe shareholders should have the power to speak and the opportunity to effect change. That power should not be concentrated in the hands of a few for reasons other than economic stake.

We generally consider a dual-class share structure to reflect negatively on a company's overall corporate governance. Because we believe that companies should have share capital structures that protect the interests of non-controlling shareholders as well as any controlling entity, we typically recommend that shareholders vote in favor of recapitalization proposals to eliminate dual-class share structures. Similarly, we will generally recommend against proposals to adopt a new class of common stock.

With regards to our evaluation of corporate governance following an IPO or spin-off within the past year, we will now include the presence of dual-class share structures as an additional factor in determining whether shareholder rights are being severely restricted indefinitely.

When analyzing voting results from meetings of shareholders at companies controlled through dual-class structures, we will carefully examine the level of approval or disapproval attributed to unaffiliated shareholders when determining whether board responsiveness is warranted. Where vote results indicate that a majority of unaffiliated shareholders supported a shareholder proposal or opposed a management proposal, we believe the board should demonstrate an appropriate level of responsiveness.

## SUPERMAJORITY VOTE REQUIREMENTS

Glass Lewis believes that supermajority vote requirements act as impediments to shareholder action on ballot items that are critical to shareholder interests. One key example is in the takeover context, where supermajority vote requirements can strongly limit the voice of shareholders in making decisions on such crucial matters as selling the business.

## STOCK SPLIT

We typically consider three metrics when evaluating whether we think a stock split is likely or necessary: (i) the historical stock pre-split price, if any; (ii) the current price relative to the company's most common trading price over the past 52 weeks; and (iii) some absolute limits on stock price that, in our view, either always make a stock split appropriate if desired by management, or would almost never be a reasonable price at which to split a stock.

## RELATED PARTY TRANSACTIONS

Pursuant to the Code, companies may seek shareholder approval for related party transactions if it surpasses their materiality threshold. We note that the Code recommends that boards are responsible for creating Group-wide policies to govern their transactions. Moreover, the company has discretion to set a materiality threshold, which may be lowered by the SEC.

We will evaluate these transactions on a case-by-case basis. Provided that there are no transactions that demonstrate egregious or illegal conduct that might threaten shareholder value, we will generally follow management's decision to enter into these transactions. In evaluating transactions, we will follow these general principles:

- Transactions must be part of the company's ordinary course of business.
- Clear disclosure regarding the proposed transactions, including relationships between the parties, descriptions of the transactions, proposed amounts, review procedures and length of time must be provided, along with disclosure that interested parties must refrain or abstain from voting on such transactions. Where the transaction terms are partially disclosed, or no details of the transactions have been disclosed, we will recommend shareholders oppose the proposed general mandate.
- For transactions involving a major shareholder, entities affiliated with a major shareholder, or entities with overlapping directors, the transaction(s) must be related to or necessary for the ordinary day-to-day operations of the company.

## CORPORATE GUARANTEES

Companies may seek shareholder approval to provide corporate guarantees to subsidiaries and associate companies. Where shareholders are asked to approve corporate guarantees, our assessment will take the following into consideration:

- i. The overall disclosure relating to the corporate guarantees;
- ii. The relationship between the company providing the corporate guarantees and those entities receiving the corporate guarantees;
- iii. The benefits for provision of guarantees to the company itself and its shareholders as a whole, ensuring that the provision of guarantees will not only benefit select major shareholders;
- iv. The size of the corporate guarantees compared to a company's net assets; and/or
- v. The rationale for the provision of guarantees.

We will oppose proposals to provide corporate guarantees if companies do not disclose the amount of corporate guarantees it intends to grant. Similarly, where a company seeks to provide corporate guarantees to joint ventures or entities where it does not have majority ownership or operational control and other investors are not providing similar corporate guarantees, we will recommend shareholders oppose such proposals as financial risk should be shared by all investment partners. The same may be applied where a company and guaranteed entity only share common directors or common shareholders, but there is no equity relationship between the company and guaranteed entity.

For entities controlled by a company and the amount of corporate guarantees are disclosed, we will evaluate the size of corporate guarantees as a percent of a company's audited net assets, as based on the most recent audited financial statements. Where the proposed corporate guarantees and existing guarantees (if any) are less than 100% of audited net assets, we will support the provision of corporate guarantees. In contrast, where the proposed guarantees and existing corporate guarantees (if any) exceed 100% of audited net assets, we will oppose the provision of corporate guarantees.

## TRANSACTION OF OTHER BUSINESS

We typically recommend that shareholders not give their proxy to management to vote on any other business items that may properly come before the annual meeting. In our opinion, granting unfettered discretion is unwise.

# Shareholder Initiatives

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Although uncommon in the Philippines, should a shareholder proposal arise, we will evaluate it on a case-by-case basis. We generally favor proposals that are likely to increase shareholder value and/or promote and protect shareholder rights. We typically prefer to leave decisions regarding day-to-day management of the business and policy decisions such as those related to political, social or environmental issues to management and the board except when there is a clear and direct link between the proposal and an economic or financial risk for the company. We feel strongly that shareholders should not attempt to micromanage the business or its executives through the initiative process. Rather, shareholders should use their influence to push for governance structures that protect shareholders, including through director elections, and promote the composition of a board they can trust to make informed and careful decisions that are in the best interests of the business and its owners. We believe that shareholders should hold directors accountable for management and policy decisions through the election of directors.

## ENVIRONMENTAL, SOCIAL & GOVERNANCE INITIATIVES

For a detailed review of our policies concerning compensation, environmental, social and governance shareholder initiatives, please refer to our comprehensive *Proxy Paper Guidelines for Shareholder Initiatives*, available at [www.glasslewis.com](http://www.glasslewis.com).

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