

## BRAZILIAN STEWARDSHIP CODE

The crisis of the international financial market in 2008 has given rise to intense debates about the best ways to prevent events that significantly impact the real economy. Under the understanding that capital markets are essential for economic development, institutional investors, whether asset managers or pension funds, play a fundamental role in the process of improving sustainable practices.

The engagement between shareholders and investee companies is still not a common practice in Brazil. There are several explanations for this cultural gap, but perhaps the main one is related to the stage of development of the Brazilian capital market. Amid this context of engagement, stewardship translates into the view that the relationship between companies and institutional investors must be guided by governance practices and principles that reflect business sustainability and the responsibility of shareholders.

Institutional investors - due their size and relevance - should play a central role in defending the sustainability of the financial market. In 2016, we took an important step forward in our commitment to raise this cause in the Brazilian capital market by launching the AMEC Code with seven investment principles to be followed by institutional investors.

Over the past five years, the voluntary adoption of the code has provided benefits to many signatories in the country. Although much has been achieved, it is clear that more should be done to accelerate the adherence to this concept by a greater number of agents.

One of the main barriers to joining the code lies in the fact that many Brazilian asset managers do not have the structure to establish long-term relationships with companies, especially considering that many assets will not last longer than a year in their portfolio.

However, an investor is not expected to maintain engagement with all the companies in their portfolios.

Not even the most sophisticated asset managers in the world do that, evidencing the need to establish some criterion of costs and benefits or the definition of discretionary choices, which is known as materiality of assets.

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In this context, we understand that institutions with structures of different sizes can develop active ownership practices, and these actions concern the presentation of annual stewardship reports.

### OBJECTIVES

By launching this Brazilian Code, AMEC and the CFA Society Brazil aim to develop and disseminate the Stewardship culture in Brazil, promoting a sense of ownership in institutional investors and creating standards for responsible engagement. The group understands that the development of stewardship activities by institutional investors will promote the adoption of good corporate governance practices and will create value for companies, as more active investors will lead companies to have better structured processes for managing their businesses and mitigating its various risks.

The Brazilian Code privileges essence over form and is therefore based on principles: a compass, not a prescription. The efficiency of prescriptive codes has been questioned as they seem to have created the “box ticking mentality,” what makes the adherence to them superficial, with few results in practical terms. The intention is to initiate a process of changing the culture of management and ownership of securities over time. For this reason, during the initial implementation stage of the Brazilian Code, there will be no sanctioning activities for the investors that adhere to it. If necessary, the Code’s governance structure may adopt educational measures in order to clarify the real meaning of the Principles.

In this sense, the Brazilian Code is not a rigid list of rules. It comprises 7 principles to be presented hereinafter and detailed in the Brazilian Code Implementation Manual that will be launched later. The Manual will make recommendations about the application of the principles.

The Brazilian Code does not intend to create new compliance obligations for institutional investors. Instead, it should lead to the creation of a unique internal document that can be eventually further developed depending on each signatory’s organizational structure. The policies mentioned herein, especially those related to internal controls and conflicts of interest, are already part of the current and most updated regulatory and self-regulatory requirements of institutional investors.

## PRINCIPLES OF THE BRAZILIAN STEWARDSHIP CODE

For the purposes of the Brazilian Code, stewardship embodies the careful management and monitoring of securities owned by the end beneficiaries, that is, the clients. Such careful management and monitoring will be outlined in this Brazilian Code through its 7 principles. The management of funds is an activity that demands trust, which is consolidated through the adoption of stewardship practices. Accordingly, to meet their fiduciary duty towards the end beneficiaries, institutional investors should:

1. Implement and disclose a stewardship program
2. Implement and disclose mechanisms to manage conflicts of interest
3. Take ESG factors into account in their investment processes and stewardship activities
4. Monitor the issuers of invested securities
5. Be active and diligent in the exercise of their voting rights
6. Establish collective engagement criteria
7. Be transparent as to their stewardship activities stewardship is the care in managing and monitoring the securities held by the final beneficiaries, the clients.

## PRINCIPLES OF THE BRAZILIAN STEWARDSHIP CODE

### PRINCIPLE 1

*Implement and disclose a stewardship program*

Institutional investors should implement a stewardship program establishing clear and objective parameters about when and how their stewardship activities will progress.

### GUIDANCE

Stewardship is an evolutionary process, a long-term planning initiative with clear goals and not a decision with immediate effects. To establish the stewardship activities to be developed and how the exercise of these activities will progress. To establish how the guidelines chosen for the interaction between institutional investors and the issuers of securities will create value for end beneficiaries and protect them. To provide stakeholders with visibility as to their stewardship program and make its implementation feasible in relation to all stakeholders, including but not limited to the clients and the issuers of securities.

### PRINCIPLE 2

*Implement and disclose mechanisms to manage conflicts of interest*

Institutional investors should establish mechanisms to manage conflicts of interest and ensure they are fully applied in the scope of their stewardship activities.

### GUIDANCE

The fiduciary duty of institutional investors is to act based on the interest of end beneficiaries. However, conflicts of interest are common in the interaction with the issuers of securities. These conflicts can take place between the institutional investors and their end beneficiaries, between institutional investors' several business segments, between the institutional investors and the invested assets and also between the end beneficiaries themselves. The decision to vote in the shareholder meeting is an example of possible conflicts of interest. Institutional investors should always manage these conflicts by indicating the necessary measures so that the interests of their end beneficiaries prevail, subject to legal provisions, especially the Article 115 of the Corporate Law 6.404/76. Institutional investors should be able to show that stewardship activities are protected against pressures and conflicts of interest.

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## PRINCIPLES OF THE BRAZILIAN STEWARDSHIP CODE

### PRINCIPLE 3

*Take ESG factors into account in their investment processes and stewardship activities*

Institutional investors should integrate environmental, social and governance factors into their investment process, evaluating both their impact on risks and returns and their contribution to the sustainable development of the issuers of securities.

#### GUIDANCE

The ESG factors impact on the issuers of securities and significantly affect their sustainability. The analysis and monitoring of ESG factors are part of the evaluation of the risks and opportunities associated with the investments, although they are not the final drivers for an investment decision. By carefully managing the assets of their end beneficiaries, institutional investors should consider relevant ESG factors as crucial aspects when it comes to the fulfillment of their fiduciary duty, being duly transparent about the way these factors will be considered. Investors should evaluate the view of the issuers of securities about relevant ESG topics.

### PRINCIPLE 4

*Monitor the issuers of securities*

Institutional investors should monitor the issuers of securities.

#### GUIDANCE

Investors should define their level of engagement with the issuers of securities, outlining if, when and how they will communicate with them to seek a clear position and the adoption of the necessary measures in relation to key issues. To define the progress of the investor knowledge about key issues related to the issuers of securities. Examples of key issues: strategy, compensation, policy on the nomination of directors, mapping and monitoring of the risks incurred in the corporate activities and ESG policies. The interaction between institutional investors and the issuers of securities should be reported in internal documents.

## PRINCIPLES OF THE BRAZILIAN STEWARDSHIP CODE

### PRINCIPLE 5

*Be active and diligent in the exercise of voting rights*

Institutional investors should actively and diligently exercise their voting rights in the issuers of securities. Votes should be duly reported, as well as the justification for the non-exercise of voting rights.

### GUIDANCE

Diligent stewardship practices culminate in the conscious exercise of voting rights. Far from being an end in itself, voting rights are the way through which securities holders play their role in the corporate governance structure of their investees. The non-diligent exercise of voting rights proportionally and negatively affects the checks and balances of issuers, impacting on their performance and, consequently, on end beneficiaries.

To exercise political rights with diligence – and especially the voting rights of the invested assets and the behavioral posture to be demanded from institutional investors so that they can appropriately meet their fiduciary duties. The non-exercise of such rights, therefore, should be an exception, duly justified and documented. This understanding should be part of the institutional investor's investment policy. Institutional investors should actively participate in the shareholder's meetings held by the issuers of securities, justify their votes in every matter and document the internal discussion process and the decisions taken. Waivers to the active exercise of voting rights should be justified, even if on an aggregate basis.

### PRINCIPLE 6

*Establish collective engagement criteria*

Institutional investors should create collective engagement conditions with other investors when appropriate

### GUIDANCE

In specific cases, the collective engagement is the most efficient form of communication between investors and the issuers of securities as it increases the legitimacy of the topics one wants to influence and optimizes costs and risks for all stakeholders. Institutional investors should define the situations in which they will act together with other invested securities holders, clarifying whether they will play an active or passive role in this interaction.

## PRINCIPLES OF THE BRAZILIAN STEWARDSHIP CODE

### PRINCIPLE 7

*Be transparent as to their stewardship activities*

Institutional investors should disclose the stewardship activities they will develop and how the progress in the exercise of such activities will be performed and disclosed.

### GUIDANCE

Investors should announce their adherence to the Brazilian Code and report the activities regulated herein and the relevant developments as to the adherence to each principle of this Code on a periodical basis.