

Carta/AMEC/Presi nº 07/2016

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Re: Contributions to ISS's Proxy Voting Guidelines for Brazil

Dear friends,

I write you as the CEO of AMEC – the Brazilian Association of Capital Market Investors. Our Association was created on October 26th 2006 by a group of institutional investors – both independent and linked to financial groups. Its main goals are the protection of minority shareholders' rights, and development of Brazilian stock markets. Over its 10 years of operation, AMEC has become the most important forum for institutional investors in Brazil on matters related to corporate governance practices and shareholders' rights.

AMEC's opinions have achieved recognition among investors, companies and regulators for its content and independence. Today our membership is comprised of 59 institutional investors– both local and foreign – with an AUM in Brazilian equities of approximately BRL 500 billion.

Over the past few years, AMEC has engaged with ISS on a number of situations, including both company-specific and systemic cases. Maybe one of the most evident situations was during our engagement with Petrobras, that resulted not only in significant corporate governance improvements at the company, but also in a true revolution in proxy voting in Brazil – both via regulation and better market practices. Another example is our letter to you, dated April 29th 2015 ([Carta Presi 03C-2015](#)), in which we voice our concerns over ISS's endorsement of the Gol restructuring, that in

practice allows the controlling shareholder to retain control with a mere 1.4% of the equity, by means of a creative and highly distortive dual-class share structure.

Our goal with this letter is manifold. First, we want to avoid situations similar to Gol, by means of a healthy exchange of experiences between ISS and AMEC. Second, we hope to strengthen our communications, especially to feed you with our most up-to-date concerns related to corporate governance and, more specifically, the voting agendas at our companies. Finally, we want to keep working with you in order to further improve the proxy voting process and all other aspects related to our capital markets.

In other words, please take the comments below as a constructive collaboration, based on the experience of our members. We are ready to discuss any of the items (and others that may be of interest to you at any time).

We also note that we hope to count on ISS in one of our forthcoming events. It was a pity that you could not participate in our Workshop on Shareholder Meetings that took place in June. I am sure that we will have more such opportunities in the future.

Best regards,

MAURO RODRIGUES DA CUNHA
CEO

CONTRIBUTIONS TO ISS VOTING GUIDELINES - BRAZIL

1. Our membership considers most of your recommendations to be well explained in your reports. However, there was a general feeling that your guidelines for Brazil are very brief, demanding many decisions on a case-by-case basis. While this may certainly be the best approach in many cases, we feel that companies and investors could benefit from a more detailed guideline – especially in controversial and YES-NO decisions, as we shall see below.
2. Members who have engaged with ISS report that your team may benefit from a bigger size – especially as bottlenecks may appear during proxy voting season.
3. On Page 4, we disagree with the idea that approving audited financials be a matter of routine. In Brazil, a unanimous approval of financial statements in effect release management from liabilities related to that year. Therefore, if investors have issues, even remote, about some management actions in the year, they should carefully ponder whether they should vote in favor of the financial statements, with votes AGAINST, ABSTAIN or WITH RESERVATIONS as alternative courses of action.
4. On the same page, we understand that minority shareholders SHOULD NOT VOTE on the election of candidates submitted by the controlling shareholders for the Fiscal Council. They should vote on the minority candidates only.
5. Still on Page 4, on the matter of dividends, Brazilian investors are more concerned with situations in which dividends are wrongly withheld than situations of excessive dividends. Your analysis should consider this.
6. Still on Page 4, we do not see a reason to vote against stock dividends, as they are usually excluded from the minimum (cash) dividend calculations.
7. On Page 5, we do not understand your opposition to “lower disclosure threshold”. Our members have never seen such a proposal.
8. On the same page, on the issue of Board Elections, we believe that your reports should include recommendations for both scenarios, ie, slate voting, separate voting or multiple voting. Also, global clients not familiar with the multiple

voting procedures could benefit from specific education and scenario analysis in your reports, on a company by company basis. More specifically, investors willing to elect independent should be instructed not to waste votes on incumbent candidates, both under the multiple voting and the separate voting methodologies.

9. Since the multiple voting process can be requested up to 48 hours before the meeting, voting instructions should ideally read “if the voting process is SLATE, we recommend voting for XXXXX; in case of separate voting, we recommend voting for XXXX; in case of multiple voting, we recommend allocating votes in the following manner (percentage of vote for each candidate). This is aligned with the new Brazilian proxy card, that will be effective in 2017.
10. Especially given Instruction 561, we anticipate petitions for multiple voting to be more timely in coming years, and count on broader support. Your guidelines should recognize this evolution, and indicate ISS’s best efforts to recommend individual candidates.
11. Additionally, you must take into account that, with the new proxy card mandated by CVM Instruction 561, investors will have to opine on the adoption of multiple voting. It will be a standard field on the card, opening an important new decision to be made. We urge you to include in your guidelines a default recommendation to vote FOR the adoption of the multiple voting system under this new option, as it improves the chance of the election taking place on a seat by seat basis, thus improving the odds to elect independent candidates.
- 12.
13. We also suggest that ISS specifically commits to a “best effort” approach to receive and analyze independent/dissident candidates, publicly indicating the hard deadline for the names to be made available prior to the meeting in order to be considered.
14. On Page 7, we suggest a reflection on the concept of independent director as applied in Brazil. Most of the times there is a strong difference in the degree of independence of a director nominated by management/controlling shareholder when compared to independent directors nominated by minority shareholders. Your guidelines and recommendations should take that into account, so that we have board populated by directors who fit more than a nominal definition of independence.

15. Along the same lines, we suggest that you review upwards the number of years of “distance” from the company and/or the controlling shareholder to gain independence status.
16. We recommend that you consider, for controlled companies, the minimum of 2 independent directors – preferably nominated by minorities. This is in line with BM&F Bovespa’s proposal to update the rules of the Novo Mercado, and stem from the fact that a lone director has a much weaker voice than if he has another independent peer in the room.
17. The USD 10k per year limit on professional services rendered could be rephrased in a way to address materiality for either the company and the director.
18. You should consider withholding votes for directors that are bound by registered shareholder’s agreements. In some companies, these directors have to vote according to instructions given to them by signatories of such agreements – defeating the purpose of the very existence of a board of directors.
19. On Page 9, we recommend that you reflect on the situation of a CEO of Company A that becomes Chairman of Company B, taking into account (1) conflicts of interest; (2) time commitment; and (3) the feasibility of holding such leading roles in two listed entities.
20. On Page 9, we recommend that you consider a policy to vote against director indemnification provisions that are too broad, effectively rendering them unaccountable. One example is the case of Oi in 2013/2014.
21. On the same page, we recommend flexibility for proposals to increase board terms to up to 2 years (if originally set at 1 year), which is considered best practice in Brazil. Our members believe that a 1-year term is too short.
22. On Page 10, our membership believes that authorization for capital increases of up to 100% without a shareholder vote are excessive. We consider it best practice for rights issues to be brought to a shareholder meeting when needed. However, for special cases that require flexibility, an authorized capital of up to 30% above the existing capital base might seem adequate.

23. On Page 10, we strongly suggest that you review your policy on dual-class shares. While we agree with the existing language in your guidelines, it has proved insufficient to warrant a vote against the most egregious proposal in this area of recent: the case of Gol Airlines. Any creative attempt to create or simulate dual-class share structures or other mechanisms that distort the relation between voting power and economic interest should be clearly opposed.
24. On Page 11, our members frown on reissuance of repurchased shares, as it may indicate attempts of market timing. They believe that repurchase programs must be either for share cancellation or to fund stock options programs.
25. On Page 12, we recommend that you consider voting against compensation for the board of directors or to the supervisory council that are too low. This is a strategy that many companies use to discourage first-class professionals to seek positions on their boards, thus filling the room with complacent friends that are not interested, or do not have the skills, to fulfill their fiduciary duties.
26. One issue that appeared on the 2016 season is that of compensation packages that are voted down, only to be approved in the same meeting with slight changes. We suggest that, if you recommend voting against a compensation package that you clients vote NO to ANY PACKAGE that is presented in the meeting itself, and thus not subject to due scrutiny by investors voting by proxy. We have seen situations of pay packages approved by a small number of shareholders physically present, given that those voting by proxy abstained in this new proposal, as they had no specific voting instructions. AMEC believe that if shareholder voted NO, any new proposal needs to be submitted in time to be voted against – and not to strategically exploit abstentions. In fact, our membership suggests that this practice be adopted for all votes – not just those related to executive pay. In other words, given a recommendation to vote against any item of the agenda, should a competing proposal be presented at the meeting, ISS should instruct its clients to vote against that proposal as well, on the grounds that it has not been properly disclosed or analyzed.
27. On Page 13, we recommend that you consider voting against stock option plans that give the board or the committees too much freedom on variables that are key to the plan's value (such as strike price, repricing parameters, vesting periods, lockups, etc.).

28. On Page 14, the matter of expansion of business activities should be treated with care. Particularly when it is submitted as a Capital Expenditure Budget, the item warrants reflection. This is the instrument thru which shareholder approve capex based on retained earnings. It is very hard to hold management accountable for squandering corporate assets – such as in the case of Petrobras – if shareholders approve the capital budget without question. We recommend a case-by-case approach.

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