



31 July 2015

Brazilian Institute of Corporate Governance
Public Hearing
Code of Best Practices of Corporate Governance

By email: codigo2015@ibgc.org.br

Thank you for inviting the International Corporate Governance Network (“ICGN”) to provide feedback to the Public Hearing on the Code of Best Practices of Corporate Governance conducted by the Brazilian Institute of Corporate Governance (IBGC).

ICGN was founded 20 years ago and is an investor-led membership organisation of more than 650 individuals based in 47 countries from around the world, including Brazil. Our mission is to inspire and promote effective standards of corporate governance to support the sustainable value creation of companies and to advance efficient markets and economies world-wide. Our members represent institutional investors with global assets under management in excess of US\$26 trillion. Accordingly, ICGN's members offer a source of practical knowledge and experience with regard to governance and investment issues. For more information on the ICGN, please visit www.icgn.org.

As you may be aware, the membership of ICGN has vetted and adopted a series of guidance principles and best practice documents on corporate governance. In particular, with regard to this Public Hearing in Brazil, we highlight the ICGN Global Governance Principles, which reflect ICGN’s positions on principles of good governance for corporate issues and principles of responsible investment practices by institutional investors.

We would like to congratulate IBGC on the thoughtful consultation document on which it is basing the review of the Code’s next edition. Our approach to this consultation is to respond to the specific questions outlined in the Highlighted Themes.

Basic Principles of Corporate Governance

Questions 1 and 2: The principles of Transparency, Fairness, Accountability and Corporate Responsibility are all important principles of good corporate governance

that we believe remain relevant. Establishing Ethics as a standalone principle may also have merit, but in many ways the four existing principles, if undertaken in appropriate spirit, should in many ways encompass ethical business practices by companies. Before establishing a new Principle, such as Ethics, the IBGC should therefore consider what specific aspects of ethics may be missing from the four existing Principles.

We note that comment is sought on the issue of “Responsibility of Government Agents”. ICGN believes that a code of responsible investment practices by institutional investors—particularly for those institutional investors (asset owners and asset managers) acting as stewards for end beneficiaries including pensioners, holders of insurance policies or private savers. A stewardship code for investors is a logical counterbalance to a code of corporate governance for companies as issuers of equity and debt securities. In most jurisdictions stewardship codes are separate documents than corporate governance codes. In this sense it may make sense for a stewardship code in Brazil to develop under a separate process.

Having said that, the Principles might anticipate the development of a stewardship code by calling for board directors—in particular independent non-executive directors—to meet with and engage with the company’s leading institutional shareholders. Even without a formal stewardship code in place, investor engagement with company directors is something to encourage, particularly with regard to issues relating to strategy, shareholder rights, financial policy and succession planning. This is particularly important for controlled companies to ensure that directors have a clear perspective on the interests of core long-term institutional investors.

The Concept of One Share=One Vote

Questions 3 and 4. We would support Concept 1, as this is less ambiguous and clearly establishes the importance of voting rights matching economic interests. We believe the text in the 4th edition remains relevant. Differential voting rights should be discouraged in the Code, and the language in the 4th edition expresses this adequately. You may wish to add that the burden should always be on the advocate of differential voting rights to show how the objectives are legitimate and cannot be achieved by other means.

Question 5. The main risk to differential voting rights is entrenchment of the controlling owner. This can marginalise minority investors, serving as an effective antitakeover mechanism. In a financial context differential voting rights can effectively provide for a costless transfer of a control premium to controlling shareholders from minority holders. In a capital markets context this amounts to a

transfer of wealth away from minority shareholders. In cases where differential ownership rights exist there should be greater protections for minority shareholders in cases of a change in control. A particular risk is the extent to which the agenda of the entrenched controlling shareholder conflicts with the interests of minority shareholders. This could relate to a number of key points, including succession planning, strategy and financial policy.

Time Availability (Board Member)

Questions 6 and 7. ICGN believes it is important for board directors to ensure they have sufficient time to fulfil their duties on the board. But we would recommend a principles-based approach rather than prescriptive rules. We agree that overboarding is a potential concern, but ICGN's Global Governance Principles do not set a specific limit for board seats. While there is a risk of overboarding without a maximum limit, there are also potential problems in setting a specific limit that works in all situations. Developing a list of considerations for the board to adopt in assessing cases of overboarding may provide a useful tool for board members in assessing individual cases.

Directors Alternates

Questions 8-10. ICGN shares the views of IBGC that alternate directors are not a good governance practice. Providing language in the Code about this might implicitly suggest that this is an acceptable governance practice. Alternative directors should be discouraged, but if they are appointed they should not receive separate compensation unless they become formal members of the board. If a position goes vacant, the board should seek that the vacant position is filled by a viable candidate who is in a position to serve a normal tour of duty on the board – not just until the next annual general meeting.

Independent Directors

Question 11. While ICGN normally supports principles-based guidelines rather than prescriptive ones, we appreciate the importance of encouraging director independence in Brazil. Accordingly, we think recommendations about what constitutes independence – and non-independence—may be sensible for the Brazilian Code.

Board Compensation

Questions 12-14. ICGN does not advocate variable, performance-based compensation to non-executive directors so that conflicts of interest can be avoided and non-executives maintain focus on the long-term success of the company. However, part or all of their director fees can be in the form of restricted stock fully vested on the grant date, but still applicable to long-term holding periods.

Variable compensation can be appropriate for executive directors, as long as it is properly structured, with appropriate performance metrics over a time frame that aligns with the interest of long-term minority shareholders. There are risks associated with variable compensation if the remuneration structure is inappropriate. These can be mitigated by an independent remuneration committee and by shareholder advisory votes on remuneration. Remuneration structures will normally differ between executive and non-executive directors. While non-executive directors warrant fees for their contribution, it may be appropriate to provide additional fees for independent non-executive committee chairmen. The board may also wish to consider if there is merit in offering additional compensation to non-executive directors for committee service.

The Fiscal Council

Questions 15 and 16. ICGN recognises that Fiscal Councils play an important role in Brazilian corporate governance structures, and in protecting the interests of minority shareholders and other providers of risk capital. While we recognise this structure is the norm within Brazil we would not recommend a permanent Fiscal Council for any type of organisation—at least to the extent that might preclude other forms of financial oversight in the governance process. Our own Global Governance Principles speak to the important role of independent audit committees on the board serving in a similar financial control function as the Fiscal Council.

While there may be merits to both the Fiscal Council and audit committee approaches, ICGN believes that it can be healthy and important for those undertaking this financial oversight function also to be part of the board as a whole and aware of all the board's considerations. But given the importance of protecting minority shareholder rights relative to controlling shareholders, we believe Fiscal Councils are likely to remain a key feature of most company governance structures, at least in the near to medium term.

We hope that these comments are useful in your deliberations and the ICGN Policy Director, George Dallas (george.dallas@icgn.org) would be happy to elaborate on any of the points raised in this letter. Thank you for your consideration.

Yours truly,

Erik Breen
Chairman
International Corporate Governance Network
Erik.Breen@triodos.nl

ICGN contacts:

Kerrie Waring, Executive Director, ICGN: kerrie.waring@icgn.org
ICGN contacts:

Carol Nolan Drake, Co-Chair ICGN Shareholder Responsibilities Committee:
drake@opers.org

Niels Lemmers, Co-Chair ICGN Shareholder Responsibilities Committee:
nlemmers@veb.net