PROXY PAPER™

GUIDELINES

2016 PROXY SEASON

AN OVERVIEW OF THE GLASS LEWIS APPROACH TO PROXY ADVICE

GERMANY

GLASS LEWIS

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Guidelines Introduction

These guidelines are intended to supplement Glass Lewis' Continental European Policy Guidelines by highlighting the key policies that we apply specifically to companies listed in Germany and the relevant regulatory background to which German companies are subject, where they differ from Europe as a whole. The Continental European Policy Guidelines describe the underlying principles, definitions and global policies that Glass Lewis uses when analysing German companies in accordance with best practice standards for Germany.

Where a topic is not addressed in these guidelines, but is addressed in the Continental European Policy Guidelines, we consider our policy approach and the relevant regulations and recommendations to be substantially the same in Germany as in continental Europe. Wherever our policy deviates from the Continental European Policy Guidelines, we will clearly state this.

CORPORATE GOVERNANCE BACKGROUND

The German Stock Corporations Act (Aktiengesetz) provides the primary legislative framework for German corporate governance. Best practices are centered on the recommendations contained in the German Corporate Governance Code ("Kodex") that operates on a comply or explain basis, whereby the management and supervisory boards of all publicly-listed companies are required to make annual statements detailing their adherence to the Kodex.

Corporate governance principles in Germany are generally less prescriptive than in many other European countries, with a strong emphasis on corporate flexibility. The Kodex contains very general provisions, which are much less specific in nature than the recommendations contained in corporate governance codes of most other European markets. The Commission of the Kodex states that the aim of the country's distinct governance code is increased transparency for investors and the strengthening of confidence in management. The Kodex, initially adopted on February 26, 2002, was most recently amended on May 5, 2015.

SUMMARY OF CHANGES FOR THE 2016 GERMANY GUIDELINES

Following is a summary of the significant changes to our 2016 Germany guidelines:

BOARD DIVERSITY

We have updated our guidelines in order to reflect recent German legislation that will impose a binding gender quota on the supervisory boards of large public companies and will require all publicly-listed German companies to set targets for the gender diversity of their management and supervisory boards. In cases where forthcoming elections appear to contravene the gender quota provisions, we may recommend that shareholders vote against the chairman of the nominating committee. We also believe that in cases where management and supervisory board composition targets are inappropriate or poorly disclosed, a vote against the chairman of the accountable committee or the chairman of the board may be warranted.

SUPERMAJORITY VOTE REQUIREMENTS

In line with changes to our Continental Europe Policy Guidelines, we have codified an existing policy by which we will typically analyse a proposed removal or imposition of supermajority requirements from a company's articles of association on a case-by-case basis.

BOARD NOMINEE DISCLOSURE

In line with changes to our Continental Europe Policy Guidelines, we have revised our policy to the effect that we will recommend voting against a director nominee, rather than recommending to abstain from voting on the nominee, when the company has not disclosed sufficient information in order to evaluate the nominee's relationship to the company.

OVERBOARDING

In line with changes to our Continental Europe Policy Guidelines, we have updated our guidelines to reflect that going forward we will recommend voting against a supervisory board member who serves as an executive officer or management board member of any public company while serving on a total of more than two (previously three) public company boards and any other director who serves on a total of more than five (previously six) public company boards. We expect a chairman of any public company to reduce his or her external commitments appropriately and we may not recommend that shareholders vote against overcommitted directors at companies where the director serves as chairman. Further, we will generally refrain from recommending to vote against a board member who serves on an excessive number of boards within a consolidated group of companies or a board member that represents a firm whose sole purpose is to manage a portfolio of investments which include the company.

I. A Supervisory Board that Serves Shareholder Interest

ELECTION OF SUPERVISORY BOARD MEMBERS

Under German law, companies are governed by a two-tier board system, with the supervisory board presiding over the management board. The supervisory board[1] consists entirely of non-executive directors, while the management board[2] is composed entirely of executive directors. The management board is responsible for the day-to-day operation of the business,[3] whereas the supervisory board is responsible for appointing and monitoring the management board.[4] Alternatively, German companies may elect to incorporate under European Company (Societas Europaea, or "S.E.") law and such companies may be governed by either a single-tier or two-tier board system.[5]

Unless otherwise provided by these guidelines, provisions will apply to companies with a two-tiered board.[6]

INDEPENDENCE

In Germany, we put supervisory board members into four categories based on an examination of the type of relationship they have with the company:

1. Independent Supervisory Board Member – An independent supervisory board member has no material[7] financial, familial[8] or other current relationships with the company,[9] its executives, or other board members, except for board service and standard fees paid for that service. An individual who has been employed by the company within the past five years[10] is not considered to be independent. We use a three-year look back for all other relationships.
2. Affiliated Supervisory Board Member – An affiliated supervisory board member has a material financial, familial or other relationship with the company or its executives, but is not an employee of the company. We will normally consider supervisory board members affiliated if they:
    - Have been employed by the company within the past five years;
    - Have – or have had within the past three years – a material business relationship with the company;

1 Article 105(1) of the German Stock Corporations Act (Aktiengesetz, or "AktG"), a legally-binding document introduced September 6, 1965.
2 Article 76 of the German Stock Corporations Act ("AktG").
3 Article 76(1) of the German Stock Corporations Act ("AktG") and Article 4.1.1 of the German Corporate Governance Code ("Kodex").
4 Article 111 of the German Stock Corporations Act ("AktG") and Article 5.1.1 of the Kodex.
5 Council Regulation (EC) 2157/2001 of 8 October 2001, on the Statute for a European Company and Foreword of the Kodex.
6 Though more German companies make use of the European Company form than in any other country, the one-tier board option has not been widely utilised by German companies incorporated under European Company law.
7 "Material" as used herein means a relationship in which the value exceeds: (i) €50,000, or the equivalent (or 50% of the total compensation paid to a board member, or where no amount is disclosed) for board members who personally receive compensation for a professional or other service they have agreed to perform for the company, outside of their service as board members. This limit would also apply to cases in which a consulting firm that is owned by or appears to be owned by a board member receives fees directly; (ii) €100,000, or where no amount is disclosed, for those board members employed by a professional services firm such as a law firm, investment bank or large consulting firm where the firm is paid for services but the individual is not directly compensated. This limit would also apply to charitable contributions to schools where a board member is a professor, or charities where a board member serves on the board or is an executive, or any other commercial dealings between the company and the director or the director's firm; (iii) 1% of either company's consolidated gross revenue for other business relationships (e.g., where the supervisory board member is an executive officer of a company that provides services or products to or receives services or products from the company); (iv) 10% of shareholders' equity and 5% of total assets for financing transactions; or (v) the total annual fees paid to a supervisory board member for a personal loan not granted on normal market terms, or where no information regarding the terms of a loan have been provided.
8 Per Glass Lewis' Continental European Policy Guidelines, familial relationships include a person's spouse, parents, children, siblings, grandparents, uncles, aunts, cousins, nieces, nephews, in-laws, and anyone (other than domestic employees) who shares such person's home. A director is an affiliate if the director has a family member who is employed by the company.
9 A company includes any parent or subsidiary in a group with the company or any entity that merged with, was acquired by, or acquired the company.
10 In our view, a five-year standard is appropriate because we believe that the unwinding of conflicting relationships between former management and supervisory board members is more likely to be complete and final after five years. However, Glass Lewis does not apply the five-year look-back period to supervisory board members who have previously served as executives of the company on an interim basis for less than one year. Article 100(2.4) of the German Stock Corporations Act ("AktG") prohibits a member of the management board from serving on the supervisory board within two years of the end of the employment mandate, unless requested by a shareholder owning more than 25% of a company's total share capital.

- Own or control 10% or more of the company's share capital or voting rights;[11]
- Have served on the supervisory board[12] for more than 15 years or more than three terms, whichever is longer;[13] or
- Have close family ties with any of the company's advisers, board members or employees.

3. Inside Supervisory Board Member – An inside supervisory board member simultaneously serves as a supervisory board member and as an employee of the company. This category may include a chairman of the board who acts as an employee of the company or is paid as an employee of the company. In Germany, supervisory board members may not legally serve simultaneously as members of the management board, representatives of management and/or officers of the company.[14] As a result, insiders are very rare on German supervisory boards. However, the law allows a member of the supervisory board to serve on the management board for a transitional period, not to exceed one year, under exceptional circumstances.
4. Employee Representatives – Due to German co-determination laws, employees are entitled to have representatives[15] on the supervisory board of all public companies with at least 500 or 2,000 employees.[16] As such, employee representatives may constitute up to half of the supervisory board members' seats on a company's supervisory board.[17] Glass Lewis does not take employee representatives into account when analysing the independence of German supervisory boards. Employee representatives are not elected by shareholders.

Voting Recommendations on the Basis of Supervisory Board Independence

Glass Lewis believes a supervisory board will be most effective in protecting shareholders' interests when at least a majority[18] of the shareholder-elected members are independent. Where 50% or more of the supervisory board members are either affiliated or inside members, we typically[19] recommend voting against some of the inside and/or affiliated members in order to satisfy the majority threshold. However, we accept the presence of representatives of significant shareholders in proportion to their equity or voting stake in the company.

11 Article 5.4.1-2 of the Kodex.

12 In certain cases, we will also consider supervisory board members to be affiliates when they have served fewer than 15 years or three terms on the supervisory board if they previously served on the management board and did not have a material break in service between their resignation from the management board and their election to the supervisory board.

13 EU Commission Recommendation of 15 February 2005 on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board. Annex II. Article 1(h). While Glass Lewis makes every effort to obtain relevant information regarding supervisory board members' terms of office, this information is not often provided by German companies. As such, we will only affiliate supervisory board members for this reason when the information is provided. Otherwise, we will note that the company has not provided the relevant information. Additionally, while we will classify board members as affiliates in accordance with this standard, we will evaluate voting recommendations based on this issue on a case-by-case basis. When a board or committee does not meet the independence standards set forth in these guidelines solely as a result of a nominee's length of service on the board, we may refrain from recommending a vote against the nominee if the board or relevant committee is otherwise sufficiently independent.

14 Article 105(1) of the German Stock Corporations Act ("AktG").

15 Article 7(1) of the German Co-Determination Act (Gesetz über die Mitbestimmung der Arbeitnehmer, or "MitbestG") and articles 1(1) and 4(1) of the German One-Third Participation Act (Gesetz über die Drittelbeteiligung der Arbeitnehmer im Aufsichtsrat, or "DrittelbG"). Pursuant to Article 7(2) of the German Co-Determination Act ("MitbestG"), supervisory boards with at least six employee representatives must have at least two employee-elect members representing the relevant trade union, depending on the size of the company and its industry classification.

16 The lower threshold applies to companies bound by the German Law on One-Third Representation (Drittelbeteiligungsgesetz or "DrittelbG"), which governs companies with between 500 and 1999 employees and mandates that labour representatives comprise one-third of the supervisory board. Public companies employing 2000 or more workers are subject to the German Co-Determination Act (Mitbestimmungsgesetz or "MitbestG"), whose Article 1(1.1) grants employee representatives half of supervisory board seats. The chairman may cast a tie-breaking vote. Companies in the mining and iron and steel producing industries may be subject to the German Co-Determination Act for Companies in the Mining and Iron & Steel Industries ("Montan-MitbestG"), which does not allow the shareholder-elected supervisory board chairman to cast a tie-breaking vote, but instead provides for an additional "neutral" member elected by the shareholder and employee representatives (Article 4(1) of the Montan-MitbestG).

17 Article 7(1) of the German Co-Determination Act ("MitbestG").

18 We note that the Kodex states only that the supervisory board should have "an adequate number of" independent members.

19 With a staggered board, if the affiliates who we believe should not be on the board are not up for election, we will express our concern regarding those board members, but we will not necessarily recommend voting against the affiliates who are up for election just to achieve the majority independence threshold.

Voting Recommendations on the Basis of Committee Independence

We believe that the majority of shareholder-elected supervisory board members serving on a company's audit[20] and compensation committees should be independent of the company and its significant shareholders.[21]

Further, we believe that at least 50% of a company's audit committee should be comprised of shareholder-elect supervisory board members.[22] Given the amount and importance of the work of the audit committee, shareholders' interests should be at least equally represented in proportion to employees. We will recommend voting against any chairman of the audit committee who: (i) is also the chairman of the supervisory board, unless a cogent reason is given;[23] (ii) is not independent of the company;[24] or (iii) is a former member of the company's management board.[25]

With respect to the composition of a company's nominating committee, the Kodex recommends that such a committee be comprised solely of shareholder-elected members.[26] Glass Lewis believes that a majority of these members should be independent of company management and other related parties. However, we accept the presence of representatives of significant shareholders on this committee in proportion to their equity or voting stake in the company.

OTHER CONSIDERATIONS FOR INDIVIDUAL BOARD MEMBERS

Our policies with regard to performance, experience and conflict-of-interest issues are not materially different from our Continental European Policy Guidelines. The following are clarifications regarding best practice recommendations in Germany.

CONFLICTS OF INTEREST

We generally recommend that shareholders vote against the following:

- A supervisory board member who is on an excessive number of boards: A supervisory board member who serves as an executive officer or management board member of any public company while serving on more than two[27] public company boards and any other supervisory board member who serves on more than five public company boards typically receives an against recommendation from Glass Lewis.[28] As stated in our Continental European Policy Guidelines, we count board chairmanships as double given the increased time commitment and we may consider relevant factors such as the size and location of the other companies where the individual serves on the board, as well as attendance records, when making recommendations based on this issue. We may also refrain from recommending against the nominee if the company provides a sufficiently compelling explanation regarding his or her significant position on the board, specialised knowledge of the company's industry, strategic role (such as adding expertise in regional markets or other countries), etc. We will also generally refrain from recommending to vote against a board

20 Articles 100(5) and 107(4) of the German Stock Corporations Act ("AktG") require that at least one member of the audit committee be an independent financial expert. However, as the law does not contain a strict definition of independence, some audit committees do not include any members classified as independent by Glass Lewis.

21 EU Commission Recommendation of 15 February 2005 on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board. Annex I. Articles 3.1 and 4.1. We believe a majority of compensation committee members should be independent of the company and shareholders owning at least 50% of the share capital or voting rights. Given the importance of the audit committee's work, we believe that a higher level of independence from major shareholders is necessary. As such, we believe a majority of audit committee members should always be independent of the company and shareholders holding more than 20% or more of the company's share capital or voting rights. While we generally believe that a majority of the members of the audit and compensation committees should also be independent of shareholders owning 10% or more of the company's share capital or voting rights, we will take into account the company's ownership structure when evaluating the composition of these committees.

22 We will recommend voting against the chairman of the board when 75% or more of the audit committee is composed of employee representatives. When employee representatives comprise 50 to 75% of the audit committee, we will note our concern.

23 Recommended by Article 5.2 of the Kodex.

24 Article 5.3.2 of the Kodex.

25 Recommended by Article 5.3.2 of the Kodex. While the Kodex only recommends that a two-year look-back period be applied to this situation, Glass Lewis believes that a five-year look-back period is more appropriate in order to protect the interests of all shareholders.

26 Article 5.3.3 of the Kodex.

27 Article 5.4.5 of the Kodex specifies a limit of three.

28 Article 100(2) of the German Stock Corporations Act ("AktG") prohibits supervisory board members from serving on more than ten supervisory boards of any incorporated companies that are legally required to have a supervisory board, although up to five additional directorships are allowable for group companies. The law further specifies that the chairman of a supervisory board may not serve on more than five incorporated company boards. We generally consider only public company boards when making voting recommendations based on this issue.

member who serves on an excessive number of boards within a consolidated group of companies or who represents a firm whose sole purpose is to manage a portfolio of investments which include the company.

- Interlocking supervisory board memberships: Former CEOs or other management board members who serve on each other's supervisory boards create an interlock that poses conflicts that should be avoided to ensure the promotion of shareholder interests above all else.[29]

BOARD STRUCTURE AND COMPOSITION

Our policies with regard to board-level risk management oversight and board diversity are not materially different from our Continental European Policy Guidelines. In deviation from our Continental European Policy Guidelines, we apply different standards for the election of former management board chairmen to the supervisory board and board size.

SEPARATION OF THE ROLES OF MANAGEMENT AND SUPERVISORY BOARDS

Glass Lewis believes that fully separating the roles of the management and supervisory boards creates a better governance structure. By law, members of the supervisory board cannot simultaneously serve as management board members, authorised representatives of the management board or company, or officers of the company,[30] except for a one-year transitional period under extraordinary circumstances.[31] Moreover, German law stipulates that former members of the management board may only serve as members of the supervisory board within two years after the end of their appointment if they are appointed by a motion presented by shareholders holding more than 25% of the voting rights in the company.[32] Lastly, in accordance with best practice standards in Germany, no more than two former members of a company's management board should serve on the supervisory board.[33]

Despite statements in German law and the Kodex cautioning against crossover between the management and supervisory boards, it was common practice until recently for German companies to appoint former management board members or executives to the role of chairman of the supervisory board. Given that the purpose of the supervisory board is to provide independent oversight of the management board,[34] we strongly believe that an independent chairman can better oversee executives and set a pro-shareholder agenda without the management conflicts that a former CEO, executive, or management board member often faces. Such oversight allows for a more proactive and effective supervisory board that is better able to protect the interests of shareholders.

We do not recommend that shareholders vote against former CEOs, executives or management board members who serve on or chair the board, unless the board is not sufficiently independent. However, we typically apply extra scrutiny to former executives who are proposed as candidates for election to the supervisory board. In line with best practice standards in Germany, we will generally recommend voting against the election of a current or recent[35] member of the management board to the supervisory board unless one of the following criteria are fulfilled: (i) the company states that the nominee will not serve as chairman; or (ii) the company provides a compelling rationale for why the nominee's service as chairman of the supervisory board will support shareholder value creation, and the board is otherwise sufficiently independent. We generally encourage our clients to support the appointment of an independent chairman whenever that question is posed in a proxy.

SIZE OF THE SUPERVISORY BOARD

While we do not believe there is a universally applicable optimum board size, we do believe boards should have at least six supervisory board members (or three supervisory board members in the event of small-cap companies) to ensure sufficient diversity in decision-making and to enable the formation of key board committees

29 We will apply a two-year look-back period to this situation. This only applies to public companies. Article 100(2.3) of the German Stock Corporations Act ("AktG") prohibits interlocking relationships in which current executives serve on each other's boards.
30 Article 105(1) of the German Stock Corporations Act ("AktG").
31 Article 105(2) of the German Stock Corporations Act ("AktG").
32 Article 100(2.4) of the German Stock Corporations Act ("AktG").
33 Article 5.4.2 of the Kodex.
34 Article 5.1.1 of the Kodex.
35 We will consider any individual serving on the management board within the past two years as "recent."

with independent supervisory board members. Under German law, the maximum supervisory board size is 21 members,[36] which we believe to be reasonable.

BOARD DIVERSITY

Supervisory Board Gender Quota

From January 1, 2016, German publicly-listed companies with 2,000 or more employees will be required to ensure that at least 30% of supervisory board seats are held by directors of each gender.[37] Companies affected by this legislation will not be required to immediately adapt the composition of their supervisory boards; rather they will be required to work toward the quota when the terms of current board members expire. Pursuant to the so-called "empty seat" provision, future elections or appointments to the supervisory board that are not in compliance with this legislation will be legally invalid and the positions will remain vacant.[38]

In principle, this quota is intended to apply to the composition of the supervisory board as a whole. However, the shareholder representatives and the employee representatives on a company's supervisory board are permitted to lodge an objection to this overall compliance provision in advance of an election, subsequent to a resolution adopted by the majority of either group.[39] Should this occur, the shareholder representatives and employee representatives will be required to each meet the quota separately. When companies subject to this legislation are proposing elections to the supervisory board, they will be required to disclose in the notice of meeting the minimum number of supervisory board seats that must be filled by directors of each gender in order to comply with the legislation as well as whether there an objection has been lodged to meet separate quotas for shareholder and employee representatives.[40]

Given the consequences of board seats initially remaining empty if companies subject to the 30% quota fail to comply with the legislation, Glass Lewis may recommend voting against the chairman of the nominating committee if forthcoming elections appear to contravene the gender quota provisions and no compelling justification is provided.

Board Diversity Targets

As a result of the aforementioned legislative developments, the supervisory boards of all German publicly-listed companies - regardless of size or employee headcount - are required to set target levels for the participation of women in both the supervisory board and management board.[41] While companies are afforded a large degree of flexibility in setting these targets, they are prohibited from setting targets for the proportion of women on each board or management level which are lower than the current composition unless women already account for at least 30% of the members of the respective board or management level.[42] Companies will be required to report on the targets set on an annual basis as well as to disclose whether targets were met. While there will be no penalties for companies that do not meet the predefined targets, the supervisory board will be required to explain the steps that have been taken and why the targets were not reached.[43]

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36 Article 95 of the German Stock Corporations Act ("AktG") stipulates that supervisory boards consist of between three and 21 supervisory board members, including employee representatives. The total number of supervisory board members must always be divisible by three, unless one of the German Co-Determination Acts ("MitbestG") require otherwise. The law further specifies the maximum number of supervisory board members allowable as follows: (i) a maximum of nine supervisory board members for a company with market capital of up to €1,500,000, (ii) a maximum of 15 supervisory board members for a company with market capital of up to €10,000,000, and (iii) a maximum of 21 supervisory board members for a company with market capital of more than €10,000,000.

37 Article 96(2) of the German Stock Corporations Act ("AktG").

38 *Ibid.* "Fragen und Antworten zu dem Gesetz für die gleichberechtigte Teilhabe von Frauen und Männern an Führungspositionen in der Privatwirtschaft und im öffentlichen Dienst." Bundesministerium für Familie, Senioren, Frauen und Jugend. Empty seats due to non-compliance with the legislation are to be filled through a by-election or through an appointment by way of court order.

39 Article 96(2) of the German Stock Corporations Act ("AktG").

40 Article 124(2) of the German Stock Corporations Act ("AktG").

41 Article 111(5) of the German Stock Corporations Act ("AktG"). Furthermore, pursuant to Article 76(4), the management boards of all German publicly-listed companies will be required to set target levels for the participation of women in the two tiers of management directly below the management board.

42 Articles 76(4) and 111(5) of the German Stock Corporations Act ("AktG"). "Fragen und Antworten zu dem Gesetz für die gleichberechtigte Teilhabe von Frauen und Männern an Führungspositionen in der Privatwirtschaft und im öffentlichen Dienst." Bundesministerium für Familie, Senioren, Frauen und Jugend. Companies are required to set these targets by September 30, 2015. The deadlines that are to be set for reaching these targets may not exceed five years, with the initial deadline to be no later than June 30, 2017.

43 "Fragen und Antworten zu dem Gesetz für die gleichberechtigte Teilhabe von Frauen und Männern an Führungspositionen in der Privatwirtschaft und im öffentlichen Dienst." Bundesministerium für Familie, Senioren, Frauen und Jugend.

While Glass Lewis typically refrains from evaluating the appropriateness of targets for board diversity, we expect companies to provide sufficient information and a meaningful discussion relating to specific diversity targets and the company's progress against such targets, in line with emerging best practice in Germany. We believe clear disclosure on this topic to be in the best interests of all shareholders wishing to evaluate the board's composition. As such, we will evaluate the sufficiency of a company's disclosure on a case-by-case basis and, in the event that we find the disclosure to be particularly lacking, may recommend shareholders vote against the chairman of the accountable committee or, in the absence of clear disclosure of accountability for setting these targets, the chairman of the supervisory board on this basis.

SUPERVISORY BOARD COMMITTEES

German public companies are required to have at least an audit committee and recommended to have a nominating committee.[44] In the absence of an audit committee, we will recommend voting against the chairman of the supervisory board on this basis; provided, however, that this will generally not apply to small-cap companies with a sufficient number of independent supervisory board members.[45]

Our policies with regard to committee performance are not materially different from our Continental European Policy Guidelines. In deviation from our Continental European Policy Guidelines, we make an exception in Germany for boards that do not form compensation committees.

AUDIT COMMITTEE

The Kodex recommends that the chairman of the supervisory board not serve as chairman of the audit committee.[46] However, the Kodex also recommends that the chairman of the audit committee should have "specialist knowledge and experience" of accounting principles and the internal control process.[47]

COMPENSATION COMMITTEE

In Germany, compensation committees are less common than in other European countries. The Kodex does not recommend that supervisory boards form compensation committees.[48] Instead, the supervisory board as a whole fulfills the aforementioned responsibilities. As such, when assessing the performance of the supervisory board with regard to compensation policy oversight, a vote against the chairman of the supervisory board may be merited due to failure to comply with best practice in Germany (please see "Vote on Executive Compensation" section below). If, however, a company forms a compensation committee that bears more responsibility for compensation oversight than the supervisory board as a whole, we will recommend voting against the compensation committee members in place of the chairman.[49]

ELECTION PROCEDURES

Our policies with regard to election procedures are not materially different from our Continental European Policy Guidelines. The following are clarifications regarding best practice recommendations in Germany.

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44 Article 5.3.3 of the Kodex, providing the nominating committee should be composed exclusively of shareholder representatives.

45 While article 324(1) of the German Commercial Code (Handelsgesetzbuch or "HGB") requires all German corporate entities to establish an audit committee, this requirement does not apply to public companies with a supervisory board or board of directors as these bodies are already required to contain at least one member who can be classified as an independent financial expert in line with article 100(5) of the German Stock Corporations Act ("AktG"). However, the establishment of an audit committee is recommended by article 5.3.2 of the Kodex. When the supervisory board is small and sufficiently independent, and when a company explicitly states that the entire supervisory board carries out the function of the audit committee, we will not recommend voting against the chairman. When the supervisory board is small and sufficiently independent, and when a company explicitly states that the entire supervisory board carries out the function of the audit committee, we will not recommend voting against the chairman.

46 Article 5.2 of the Kodex.

47 Article 5.3.2 of the Kodex.

48 Article 4.2.2. of the Kodex stipulates that the entire supervisory board is responsible for determining and reviewing management compensation, thus rendering compensation committees ineffective. Article 87 of the German Stock Corporations Act ("AktG") sets a legal precedent for the entire supervisory board to review and approve management board compensation. In fact, all supervisory board members may be held personally liable if management board compensation is deemed inappropriate. However, Article 5.1.2 of the Kodex allows for the possibility of a separate committee being formed to negotiate the details of management board contracts and to present proposals to the supervisory board as a whole.

49 Where the recommendation is to vote against the chairman or compensation committee chair and the individual is not up for election, we do not recommend voting against any members of the supervisory board or compensation committee who are up for election; rather, we will express our concern regarding the individual.

CLASSIFIED SUPERVISORY BOARDS AND TERM LENGTHS

German law requires that supervisory board members either resign or stand for re-election at least every five years.[50] As a result, most German companies appoint supervisory board members for the full five-year term allowable by law. Until June 6, 2008, the Kodex recommended that supervisory board elections be staggered so that some supervisory board members would stand for election at regular intervals. As a result, several companies continue to maintain staggered supervisory boards. However, a majority of companies elect the entire supervisory board only every five years.

Given that it is common practice in Germany for companies to nominate supervisory board members for five-year terms, we do not normally recommend voting against candidates who are nominated for five-year terms.

ELECTION OF SUPERVISORY BOARD MEMBERS AS A SLATE

German companies are recommended to elect supervisory board members individually.[51] Given that most companies comply with this best practice, we recommend voting against any election that is clearly proposed as a slate.

PARTNERSHIP LIMITED BY SHARES (KOMMANDITGESELLSCHAFT AUF AKTIEN, OR "KGaA")

Under German law, a publicly-traded company may be both a limited partnership and a stock corporation. This unique hybrid company structure, the Kommanditgesellschaft auf Aktien, or "KGaA," is utilised infrequently in comparison with the more common German public stock corporation (Aktiengesellschaft, or "AG") structure. In general, Glass Lewis believes that the KGaA company form is not conducive to promoting accountability to shareholders or best practices for corporate governance. The structure of a KGaA creates the possibility for management, through the limited partnership, to exercise disproportionate control over a company's governance structure. Specifically, the supervisory board of a KGaA does not have the power to hire or fire management, in contrast with the supervisory board of an AG. The supervisory board's role at a KGaA is to consult with management on issues related to shareholders' interests. Given the substantially reduced supervisory board authority under the KGaA company form, Glass Lewis does not support proposals to transform a company from an AG, or other comparable legal form, to a KGaA.

Notwithstanding our unfavourable view of the KGaA from a shareholder rights' perspective, we believe that most shareholders of a KGaA both understand and accept that the structure's legal form of company differs from that of an AG, or any comparable legal form. As such, we will not apply the same independence standards to the supervisory board or committees of a KGaA that we apply to companies incorporated in a more typical stock corporation form, such as an AG. Given the varying capital structure possibilities of a KGaA, we approach each KGaA on a case-by-case basis. However, we generally believe that the supervisory board of a KGaA should reflect the company's shareholder structure. In addition, we note that the supervisory board of a KGaA is not responsible for oversight of the company's financial reporting,[52] thereby rendering the formation of an audit committee less relevant. As such, we will exempt companies incorporated in the form of a KGaA from the requirement that they form an audit committee of the supervisory board if the company has an adequately independent committee responsible for overseeing the audit of the company's financial statements within another governing body of the company. If a KGaA chooses to form an audit committee of the supervisory board, we will evaluate its composition based on the responsibilities assigned to the committee.

50 Article 102(1) of the German Stock Corporations Act ("AktG").
51 Article 5.4.3 of the Kodex.
52 Article 286(1) of the German Stock Corporations Act ("AktG").

LACK OF ADEQUATE SUPERVISORY BOARD DISCLOSURE

Disclosure of information regarding the composition of the supervisory board and the background of its members is lightly regulated in Germany and has historically been less thorough than in other major European markets. As a result, the content and quality of public disclosure regarding the board varies widely in Germany. The Kodex recommends that supervisory boards disclose the relevant personal and business relationships that board nominees have with a company, its executives and any shareholder that directly or indirectly holds in excess of 10% of that company's total share capital.[53] Glass Lewis may recommend shareholders vote against new candidates in the case where such relevant information has not been provided.

The Kodex also recommends that supervisory boards set and disclose concrete targets for their composition; specifically, the independence, gender, nationality and age of supervisory board members should be taken into account.[54] We expect companies to provide clear and consistent disclosure of these targets, with a compelling justification for any failures to meet previously stated goals.

We may recommend shareholders vote against the re-election of the chairman of the nominating committee, or in the absence of a nominating committee, the chairman of the board, if disclosure of candidates' backgrounds and relevant qualifications and/or the targets for board composition is particularly poor.

53 Article 5.4.1 of the Kodex.
54 *Ibid.*

II. Transparency and Integrity in Financial Reporting

In Germany, shareholders are presented with the audited financial statements for the past fiscal year and are asked to vote on the appointment of the statutory auditor and the allocation and the allocation of profits or dividends on an annual basis.[55] While we have outlined the principle characteristics of these types of proposals that we encounter in Germany below, our policies regarding these issues are not materially different from our Continental European Policy Guidelines.

ACCOUNTS AND REPORTS/CONSOLIDATED ACCOUNTS AND REPORTS

In Germany, a company's audited consolidated and non-consolidated financial statements must be approved by the supervisory board and subsequently presented to the management board within two months of the receipt of the independent auditor's report.[56] Following approval by the management and supervisory boards, the audited financial statements are presented to shareholders at the annual meeting, which must be held within eight months of the close of the fiscal year.[57] However, shareholders will be asked to approve the submitted financial statements under the following three circumstances: (i) when the management and supervisory boards cannot agree on the approval of the financial statements; (ii) when the management and supervisory boards decide, for any reason, that the annual meeting will have the final authority to approve the financial statements;[58] or (iii) if the company's legal form is a partnership limited by shares (KGaA).[59]

ALLOCATION OF PROFITS/DIVIDENDS

In accordance with German law, companies may choose to allocate their profits to one or more of the following categories, subject to shareholder approval: (i) a dividend paid to shareholders; (ii) revenue reserves; (iii) retained earnings; or (iv) unappropriated net profits.[60] In any case, not more than half of a company's annual profits may be allocated to revenue reserves without explicit shareholder approval.[61] Additionally, a German company's articles may contain provisions that allow management to make an advance dividend payment based on annual financial statements, up to half of the Company's reported net profits, with the approval of the supervisory board.[62]

55 Article 119 of the German Stock Corporations Act ("AktG").
56 Article 171 of the German Stock Corporations Act ("AktG").
57 Article 175(1) of the German Stock Corporations Act ("AktG").
58 Articles 172 and 173(1) of the German Stock Corporations Act ("AktG").
59 Article 286(1) of the German Stock Corporations Act ("AktG").
60 Article 170(2) of the German Stock Corporations Act ("AktG").
61 Article 58(2) of the German Stock Corporations Act ("AktG").
62 Article 59 of the German Stock Corporations Act ("AktG").

III. The Link Between Compensation and Performance

In Germany, shareholders are not entitled to a vote on executive compensation. However, the German Stock Corporations Act ("AktG") was amended on July 31, 2009, to allow for the possibility of non-binding advisory votes on executive compensation policy.[63] These votes may either be proposed by the supervisory board or requested by shareholders in the form of a shareholder proposal or countermotion. The Kodex does not currently contain any recommendations regarding a shareholder vote on executive compensation.

In addition, shareholders of German companies are regularly asked to approve changes to supervisory board fee policies and equity compensation plans for employees. Our policies regarding these matters do not differ materially from our Continental European Policy Guidelines. However, we do account for a company's compliance with best practice in Germany, as described below, when evaluating these proposals.

VOTE ON EXECUTIVE COMPENSATION ("SAY ON PAY")

Most say on pay proposals in Germany seek shareholder approval of a company's compensation policy for the upcoming fiscal year, although some proposals may ask shareholders to approve the policy applied during the past fiscal year. The Kodex sets out general recommendations for best practices regarding executive compensation. However, provisions relating to the disclosure of executive compensation are considerably more definitive. The Kodex recommends that companies disclose the following payments made to each individual management board member:

- the benefits granted for the year under review, including the maximum and minimum potential compensation for variable compensation components;
- the allocation of fixed and variable compensation (short and long-term) for the year under review, broken down into the relevant reference years; and
- the service cost for the year under review, including pension provisions and other benefits.[64]

Further, the Kodex specifies that this information should be displayed in line with the model tables provided within its annexes. Given that the Corporate Governance Commission has particularly focused on the drafting and clarification of these templates. Glass Lewis expects all German companies to comply with the standardised format unless a particularly cogent justification is provided. Absent such disclosure, we are unlikely to recommend that shareholders support a say on pay proposal.

When evaluating a company's compliance with best practices in Germany, the following deficiencies may cause Glass Lewis to recommend a vote against a compensation policy:

- Management board members do not receive performance-based variable cash or equity compensation;[65]
- Management board compensation is not linked to appropriate multi-year individual and company performance targets;[66]
- Performance goals were lowered when management failed or was unlikely to meet original goals;[67]
- Overall and individual compensation components are not subject to clearly disclosed caps;[68]

63 Article 120(4) of the German Stock Corporations Act ("AktG").
64 Article 4.2.5 of the Kodex.
65 Article 4.2.3 of the Kodex.
66 Articles 4.2.2 and 4.2.3 of the Kodex.
67 *Ibid.*
68 Article 4.2.3 of the Kodex.

- The compensation report does not contain clear disclosure detailing the component of each management board member's compensation;[69] and/or
- The supervisory board approves severance pay for a member of the management board that is more than twice his or her total annual compensation or three times his or her total annual compensation, in the case of a change of control.[70]

SUPERVISORY BOARD COMPENSATION PLANS

Under German law, supervisory board members' compensation must either be approved by a general meeting of shareholders or specified in a company's articles of association. The Kodex specifies that if compensation plans for supervisory board members includes a variable, performance-related component, it should be oriented toward a company's sustainable growth.[71] Glass Lewis does not believe that performance-based variable compensation serves shareholders' interests, as non-executive directors who receive performance-based compensation may be forced to weigh their own interests against the interests of shareholders and the company. Therefore, while we will support compensation proposals that include limited variable compensation for supervisory board members, we will recommend voting against any proposal that seeks to add or increase performance-based fees to a supervisory board members' compensation. Additionally, we may recommend that shareholders vote against any supervisory board fee policies that include variable fees based solely on short-term profit-based metrics.

Notably, each supervisory board member's compensation should be disclosed individually, with fixed and variable components accounted for separately.[72]

EXEMPTION FROM EXECUTIVE COMPENSATION REPORTING REQUIREMENTS

German companies are required to disclose each component of each member of the management board's compensation separately, unless a company's articles of association specify that executive disclosure will be disclosed as one lump sum.[73] We recommend that shareholders vote against proposals to amend a company's articles of association in order to avoid individual management board compensation disclosure.

69 Articles 4.2.4 and 4.2.5 of the Kodex. We will make an exception when a three-quarters majority of shareholders has exempted the company from disclosing management compensation on an individual basis. Articles 285 and 314 of the German Commercial Code (Handelsgesetzbuch or "HGB") require disclosure of each element of executive compensation on an individual basis; however, Article 286 of the Commercial Code allows shareholders to approve, by a three-quarters majority, an amendment to the company's articles of association that exempts companies from the requirement that executive compensation be disclosed on an individual basis for periods of up to five years, with the possibility of renewal.

70 Article 4.2.3 of the Kodex.

71 Article 5.4.6 of the Kodex recommends that performance-related compensation for supervisory board members should be based on the long-term performance of the company. We note, however, that according to the EU Recommendation on the role of non-executive directors, receiving or having received significant additional compensation, particularly in the form of participation in a share option or any other performance-related pay scheme is seen as potentially capable of compromising the independence of non-executive directors.

72 *Ibid.*

73 Articles 285 and 314 of the German Commercial Code (Handelsgesetzbuch or "HGB") require disclosure of each element of executive compensation on an individual basis; however, Article 286 of the Commercial Code allows shareholders to approve, by a three-quarters majority, an amendment to the company's articles of association that exempts companies from the requirement that executive compensation be disclosed on an individual basis for periods of up to five years, with the possibility of renewal.

IV. Governance Structure and the Shareholder Franchise

In Germany, shareholders are asked to approve proposals regarding a company's governance structure, as well as the ratification of management and supervisory board acts and amendments to the articles of association. While we have outlined the principle characteristics of these types of proposals that we encounter in Germany below, our policies regarding these issues are not materially different from our Continental European Policy Guidelines.

RATIFICATION OF SUPERVISORY AND MANAGEMENT BOARD ACTS

For up to eight months after the end of a fiscal year, German companies may request that shareholders discharge the members of the supervisory board and/or management board from any and all of their actions during the past fiscal year. Shareholders holding at least 10% of a company's share capital, or shares with an aggregate nominal value of at least €1 million, may request that individual members of the supervisory or management boards be discharged separately.

In Germany, ratifying the acts of the management and supervisory boards is primarily a vote of confidence and does not release its members from liability for their actions. They will still be held liable for any tortious or negligent act committed in the performance of their duties. In accordance with best practice in Germany, we believe the ratification of management and supervisory board acts should be presented as a separate voting item for each individual, particularly where there is no separate proposal to elect the board or where there are significant, known shareholder concerns regarding the board's performance during the past fiscal year.

OWNERSHIP REPORTING REQUIREMENTS

German law requires that any shareholder whose percentage ownership of outstanding shares or voting rights in a company rises above or falls below the thresholds of 3%, 5%, 10%, 15%, 20%, 25%, 30%, 50%, or 75% disclose their shareholdings within four trading days of the acquisition or sale.[74] The management board is then required to disclose this information to shareholders.

In addition, shareholders who cross the 10% ownership threshold are required to disclose the following information within 20 trading days of the acquisition:[75] (i) whether the acquisition was motivated by a trading profit goal or a strategic investment decision; (ii) whether the shareholder intends to acquire further voting rights in the next 12 months; (iii) whether the shareholder intends to influence the composition of the company's board or management; and (iv) the shareholder's intentions with regard to the company's capital structure and dividend policy. In addition, the shareholder must reveal the source of his or her financing for the acquisition, especially whether the acquisition was financed through debt or equity. Lastly, the shareholder must update the company if any of the four aforementioned intentions change, for as long as the shareholder maintains ownership of at least 10% of the voting rights. The company, in turn, is required to make all of the aforementioned information public.

EXEMPTIONS FROM OWNERSHIP REPORTING REQUIREMENTS

In accordance with German law, companies may request an exemption[76] from the increased reporting requirements mentioned above for shareholders who cross the 10% ownership threshold. In general, we believe that exempting certain companies from market-wide disclosure requirements may disadvantage shareholders

74 Article 21(1) of the German Securities Trading Act (Gesetz über den Wertpapierhandel or "WpHG").

75 The amended provisions of Article 27a(1) of the German Securities Trading Act ("WpHG") took effect on May 31, 2009, with the intention of protecting minority shareholders' interests.

76 Article 27a(3) of the German Securities Trading Act ("WpHG") allows companies to seek an exemption through an amendment to the articles of association approved by shareholders.

of the companies that seek such exemptions. We are especially concerned that seeking an exemption from required reporting standards may create the opportunity for management and/or major shareholders to act in their own interests to the exclusion of the interests of minority shareholders. As such, we will generally not support proposals seeking an exemption from reporting requirements, unless management provides a specific and justifiable reason and the exemption will not harm minority shareholders' interests.

RESTRICTIONS ON SHARE REGISTRATION

Under certain conditions, German companies may impose registration restrictions on shareholders who own shares through an intermediary. Companies may seek shareholder approval to amend the articles of association in order to implement one of the following restrictions:[77] (i) an absolute cap on the number of shares that may be entered into the share register under the name of a deposit institution that is not the direct beneficial owner of the shares; (ii) an absolute cap on voting rights assigned to shares registered in the name of a deposit institution; (iii) a duty to disclose specified identifying information for beneficial owners that exceed a certain threshold; or (iv) a suspension of voting rights for shareholders who do not comply with a company's disclosure requirements. In our view, shareholders should have the right to vote in direct proportion to their holdings. While we believe that shareholders should fully disclose their holdings in accordance with the law, we do not support restricting shareholders' voting rights beyond what is required by law. As such, we will not support proposals that seek to restrict shareholders' voting rights in any way.

SUPERMAJORITY VOTE REQUIREMENTS

German law requires the support of a supermajority of votes cast on certain voting decisions at shareholder meetings in order for the motion to be passed; however, we will generally recommend voting against any proposal that extends this supermajority requirement to decisions not stipulated by law, except where the relevant provision is designed to protect minority shareholders. German companies can generally establish a lower threshold in their articles of association than is required by law to approve certain voting items. In cases where a company seeks to abolish supermajority voting requirements we will evaluate such proposals on a case-by-case basis. In certain instances, amendments to voting requirements may have a deleterious effect on shareholders rights where a company has a large or controlling shareholder. We will consider a broad range of factors including the company's shareholder structure; quorum requirements; impending transactions – involving the company or a major shareholder – and any internal conflicts within the company.

77 Article 67 of the German Stock Corporations Act ("AktG").

V. Capital Management

In Germany, shareholders are regularly asked to approve capital proposals, namely increases in authorised and conditional capital, the issuance of convertible debt instruments and the authority to repurchase shares. Such authorities generally extend for five years. Our policies with regard to these matters do not differ materially from our Continental European Policy Guidelines.

AUTHORISED CAPITAL

German companies generally ask shareholders to approve an unallocated pool of authorised but unissued shares, which may be issued with or without preemptive rights.[78] Shares issued pursuant to these authorities may be used for a broad range of corporate purposes, including raising funds for expansion plans, refinancing existing loans, or carrying out mergers and acquisitions. By law, a company's authorised capital may not exceed 50% of a company's issued share capital and is valid for a maximum period of five years.[79] Best practice in Germany, although not specifically stated in any codified recommendations, provides that preemptive rights should be preserved for share issues from authorised capital in excess of 20% of issued share capital at the date of approval. As such, and in line with our Continental European Policy Guidelines, we will generally recommend voting against any authorised capital proposal which does not preserve preemptive rights above 20% of current issued share capital; further, we believe all general authorities to issue shares should have a common cap. Glass Lewis will recommend voting against any proposal that does not explicitly extend a 20% cap on share issues without preemptive rights to authorised and conditional capital authorities previously existing and/or proposed at the meeting, other than those reserved for unique purposes such as equity incentive plans.

CONDITIONAL CAPITAL

German companies may ask shareholders to approve "conditional" or "contingent" capital. These capital increases may only be used under certain specifications, such as the issuance of shares to fulfill a company's obligations to holders of convertible debt instruments or stock options.[80] By law, a company's conditional capital may not exceed 50% of a company's issued share capital and is valid for a maximum period of five years.[81] As such, we will evaluate these proposals in conjunction with the proposed authority that allows the company to utilise it. Furthermore, we will apply the same scrutiny to the preservation of preemptive rights as explained above under "Authorised Capital."

AUTHORITY TO REPURCHASE SHARES

If German companies intend to buy back shares, they are subject to the following conditions: (i) the volume of shares to be repurchased must not exceed 10% of the nominal share capital and only funds that could have otherwise been paid out to shareholders in the form of dividends can be disbursed for repurchase transactions;[82] (ii) the company must not repurchase its shares for the purpose of trading,[83] and (iii) the authority to repurchase shares cannot be granted for a period of time exceeding five years.[84] In addition, banks and financial institutions may seek approval at a general meeting of shareholders to repurchase shares for the purpose of securities

78 Article 203(2) of the German Stock Corporations Act ("AktG").
79 Article 202(2) and 202(3) of the German Stock Corporations Act ("AktG"). Article 186(3) of the German Stock Corporation Act (AktG) further limits issuances of shares for cash consideration without preemptive rights to 10% of a company's total share capital.
80 Article 192(2) of the German Stock Corporations Act (AktG).
81 Article 192(3) of the German Stock Corporations Act (AktG"). The law further limits issuances of convertible debt instruments for cash consideration without preemptive rights to 10% of a company's total share capital.
82 Article 71(1.8) of the German Stock Corporations Act ("AktG").
83 *Ibid.*
84 *Ibid.*

trading, within a limit of 5% of the company's share capital. When seeking such an approval, the highest and lowest price must be stated.[85]

Given these legal provisions, we will generally recommend supporting a proposed authority to repurchase and/or trade in shares in Germany.

85 Article 71(1.7) of the German Stock Corporations Act ("AktG").

VI. Shareholder Initiatives

In Germany, there are two types of shareholder initiatives that may be included on the agenda of a general shareholders' meeting: shareholder countermotions and shareholder proposals. Shareholder countermotions are much more common than shareholder proposals, as they can be put forward by any shareholder who submits the motion in accordance with the applicable legal requirements.[86] Countermotions must correspond to a voting proposal on the agenda for the general meeting and generally urge shareholders to vote against the proposal put forth by management. However, countermotions may also propose separate voting decisions, including the amendment of a proposal put forth by management. These proposals generally request changes to a company's dividend policy, capital authorities, or supervisory board composition. They may also request that a special audit into management or supervisory board activities be carried out.

Shareholder countermotions may or may not be proposed as separate voting items at the general meeting. In general, Glass Lewis will provide voting recommendations for all shareholder countermotions that are clearly designated as separate voting items.[87] Given the broad range of topics that may be addressed by countermotions, we will analyse each countermotion on a case-by-case basis. In general, however, we will not support countermotions that seek to manage a company's day-to-day business, which we believe is better managed by the management and supervisory boards.

In Germany, shareholders owning at least 5% of a company's share capital, or a nominal value of €500,000 in a company's shares, may request that a separate proposal be included on the agenda of a general meeting of shareholders.[88] Such requests much be submitted at least 30 days prior to the meeting date. Though shareholder proposals are rare in Germany, when submitted, they generally propose the appointment of a special auditor to investigate management or supervisory board actions, the removal of supervisory board members or the election of dissident supervisory board members.

We evaluate shareholder proposals or countermotions at German companies on a case-by-case basis. We generally favour 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 all available means to push for governance structures that protect shareholders, including through supervisory board elections to promote the composition of a board they can trust to make informed and prudent decisions that are in the best interests of the business and shareholders. We believe that shareholders should hold supervisory board members accountable for management and policy decisions through the election of board members.

86 Article 126 of the German Stock Corporations Act ("AktG").

87 Countermotions that will be voted on separately at the meeting are generally designated by a letter on the proxy form. Where such a letter is assigned, we will provide voting recommendations. We note that the statutory filing deadline for shareholder countermotions is 14 days before the meeting. As such, we are not always able to provide voting recommendations for all shareholder countermotions in advance of the vote cutoff.

88 Article 122(2) of the German Stock Corporations Act ("AktG").

DISCLAIMER

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