To: Regierungskommission Deutscher Corporate Governance Kodex

RE: Consultation on the proposed amendments to the German Corporate Governance Kodex

Glass, Lewis & Co. (“Glass Lewis”) appreciates the opportunity to comment on the amendments to the Kodex proposed by the Regierungskommission during the consultation process that commenced on November 2, 2016.

Glass Lewis is an independent corporate governance firm, providing proxy voting research, analysis and recommendations to a global client base of institutional investors. Glass Lewis is submitting this comment as an interested industry advisor, not on behalf of any or all of its clients.

Following our perusal of the consultation documents, we have identified certain proposed amendments on which we would like to pass comment, as well as current Kodex provisions to which we believe that expansion or additional clarification would be of particular benefit to market participants:

**Art. 4.2.3 - Multi-annual, Variable Compensation**

According to the amendments proposed to Art. 4.2.3, a specification regarding the time base to be used to assess multi-year compensation to executives will be introduced. In particular, the amendment clarifies that these awards shall be based on future years’ developments.

This specification appears consistent with the orientation to sustainable growth recommended by the Kodex for companies’ executive compensation structures, as well as with our view of long-term incentives. In general, we believe long-term awards should be aimed at aligning executive directors’ pay with sustainable growth and, as such, with shareholders’ interests. While the appropriate compensation structure will vary from company to company, we generally find that prospective targets to be achieved in upcoming years are more effective at incentivising executives, and more transparent for investors to evaluate, than a retrospective assessment.

Further, the Regierungskommission has proposed to add clarification on the inclusion of multi-year compensation in the severance calculation, specifying that amounts which would partially fall in said calculation shall not be “paid out ahead of schedule”.

While we are favourable of the Regierungskommission’s decision to provide guidance on a compensation topic that is often a cause for significant debate, we find that the proposed amendment in its current form would still leave some space for divergent interpretations. In particular, while recommendations regarding the timing of vesting seem to be clear, Glass Lewis believes market participants would benefit if the Kodex provided even more depth in relation to awards vesting post-termination. For example, a recommendation regarding whether awards should be pro-rated based on time served by the executive or, more importantly, a recommendation that long-term incentive awards should continue to be subject to initial performance conditions, would arguably add further depth to this provision.

We believe such a further specification would be especially valuable, considering that severance awards based on total compensation may yield higher payouts to departing executives than the regulations of many other European countries would allow. For example, while in Switzerland
severance payments have been prohibited by the Minder Initiative, in France severance payments
typically include only fixed and one-year variable compensation and are often subject to the
satisfaction of additional performance conditions.

Art. 5.2 - Tasks and Authorities of the Chairman of the Supervisory Board

We welcome clarification from the Regierungskommission that the involvement of the chairman of
the supervisory board in engagement with investors is recommended in certain circumstances. In
our view, this proposed provision pays heed to the fact that engagement is becoming an important
tool for investors and that certain issues, which are in the sole remit of the supervisory board, are
best discussed without the presence of management board members. In particular, we believe that
discussions with investors concerning management board contracts and compensation are likely to
be more fruitful when executive directors are not involved.

Art. 5.3.2 - Composition and Function of the Audit Committee

Despite changes to the requirements for the composition of the audit committee through AReG, we
find it positive that the Regierungskommission is intending to uphold the recommendation that the
chairman of the audit committee is an independent supervisory board member. In our view, given
the importance of the role of the audit committee, shareholders are best served when this
committee is led by an independent board member.

However, given the amendments to Art. 100(5) Aktiengesetz through AReG, we believe a
recommendation for companies to disclose how the supervisory board fulfils the requirement of
being familiar with the sector in which the company operates could improve transparency and assist
market participants in assessing the composition of the supervisory board and its key committees.
This recommendation could, for example, be included as part of the proposed recommendation for
the supervisory board to establish a profile of competencies in Art. 5.4.1.

Arts. 5.4.1 and 5.4.2 - Composition and Independence of the Supervisory Board

The additions proposed for Art. 5.4.1 comprise, inter alia, a recommendation for the supervisory
board to set up a “profile of competencies” for all directors on the board. We believe this
specification is in line with best practice across Europe, where the disclosure and evaluation of non-
executive directors’ skill sets is gaining increasing attention and being utilised by market participants
when assessing the overall composition of the supervisory board.

Even more importantly, we find the introduction of a provision to present the curriculum vitae of all
new candidates to the board on a company’s website, as proposed in the fifth paragraph of the
Article, to be an important step in increasing transparency. Considering the increasing frequency of
by-elections and staggered boards, whereby not all supervisory board members may be up for
election at a particular general meeting, we find it to be particularly welcoming that the
Regierungskommission proposes to recommend that up-to-date biographic information for all
incumbent supervisory board members, and not just those proposed for election, is published on
companies’ websites to assist market participants in assessing the relevant skills of individual
candidates in the context of the competence profile of the supervisory board as a whole.

Finally, we commend the Regierungskommission for the introduction of a provision recommending
that companies disclose the identity of supervisory board members that are considered independent
in the corporate governance report.
While Glass Lewis is mindful that the Regierungskommission has reached an agreement that the definition of independence in Art. 5.4.2 should not be amended, we believe that a recommendation for companies to disclose the basis on which an assessment of the independence of supervisory board members has been made would also lead to increased transparency and a more meaningful assessment of the independence of supervisory board members and overall board composition. Further, while we acknowledge the Regierungskommission's position that only a relationship with a controlling shareholder would be sufficient to compromise a supervisory board member’s independence, we believe that many market participants and investors would consider a relationship with any shareholder holding a material non-controlling interest to be of key importance in their evaluation of the composition of the supervisory board. Particularly considering that relationships with substantial shareholders often arise or cease to exist during a board member’s term, Glass Lewis believes an expansion of the provision in Art. 5.4.1 to recommend that companies disclose all supervisory board members’ relationships with substantial shareholders on an annual basis, and not just when they are standing for election, would be of benefit investors.

In our view, the expansion of this provision is unlikely to represent a major disclosure burden for companies and would likely lead to a tangible increase in transparency related to the composition of the supervisory board - a goal that we believe the Regierungskommission is attempting to pursue with many of its other proposed amendments.

Art. 5.4.6 - Compensation of Supervisory Board Members

Glass Lewis was previously in favour of the Regierungskommission's 2012 update to this provision, which saw the removal of a recommendation that supervisory board members receive performance-based compensation in addition to fixed compensation. In our view, performance-based fees may align the supervisory board’s interests with those of management, potentially compromising the supervisory board’s objectivity in carrying out its oversight functions. We believe that the removal of this recommendation has led to many companies removing variable compensation elements for supervisory board members in line with evolving international best practice.

In our view, an expansion of this provision to include a recommended cap on variable compensation (as a percentage of fixed compensation) as well as a recommendation of which metrics may be inappropriate (such as earnings per share, dividend payments, or metrics that are also utilised in executive compensation programmes) would certainly serve as a step in the right direction. However, Glass Lewis continues to believe that the elimination of performance-related fees to supervisory board members would be the most appropriate course of action.

Art. 5.4.7 - Meeting Attendance of Supervisory Board Members

We are mindful that poor attendance in one particular year may occur due to circumstances beyond a supervisory board member’s control; however, we believe that repeated and unexplained failure to attend board and committee meetings represents a fundamental failure to represent shareholders and may be a signal that a board member does not have enough time to commit to this role.

Art. 5.4.7 recommends that companies disclose whether a supervisory board member attended only half or less of the board and committee meetings held during the year. While most companies comply with this recommendation, we find that they often neglect to name supervisory board members with a poor attendance record.

Furthermore, we believe that market participants have varying standards at which they consider attendance levels to be of interest, and that many consider a recommendation of additional
disclosure for below 50% attendance as "setting the bar too low". As such, Glass Lewis is of the opinion that a full breakdown of individual attendance is a key point of reference for shareholders’ assessment of supervisory board members’ performance and ability to devote sufficient attention to the company on the whole. If disclosing a full breakdown of individual meeting attendance is considered burdensome, we believe that increasing the level at which attendance is recommended to be disclosed above one half of board and committee meetings (for example, to 75%) would be viewed favourably by many market participants and would assist them in considering the suitability of the proposed reelection of incumbent board members.

Glass Lewis welcomes the opportunity to comment on the proposed amendments to the Kodex and is available to answer any questions the Regierungskommission may have regarding the comments provided above. Additionally, Glass Lewis raises no objection to these comments being published on the Regierungskommission’s website.

Respectfully submitted,

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