



# South Africa

## Proxy Voting Guidelines

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2016-2017 Benchmark Policy Recommendations

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## TABLE OF CONTENTS

OVERVIEW.....	3
1. ANNUAL FINANCIAL STATEMENTS.....	4
2. AUDITORS' REAPPOINTMENT AND REMUNERATION.....	4
3. DIRECTOR ELECTIONS .....	4
ISS Classification of Non-Independent Non-Executive Directors.....	5
4. AUDIT COMMITTEE ELECTIONS .....	6
5. SHARE ISSUANCE AUTHORITIES.....	6
6. SHARE BUYBACK AUTHORITIES .....	7
7. FEES FOR NON-EXECUTIVE DIRECTORS .....	7
8. FINANCIAL ASSISTANCE TO RELATED OR INTER-RELATED COMPANIES .....	8
9. AUTHORITY TO RATIFY AND EXECUTE APPROVED RESOLUTIONS .....	8
10. APPROVAL OF REMUNERATION POLICY.....	8
11. NEW EQUITY INCENTIVE SCHEME OR AMENDMENT TO EXISTING SCHEMES.....	9
12. NEW MEMORANDUM OF INCORPORATION (MOI)/AMENDMENTS TO THE MOI .....	10
13. BLACK ECONOMIC EMPOWERMENT (BEE) TRANSACTIONS.....	10
14. SOCIAL AND ETHICS COMMITTEE ELECTIONS .....	11
15. SOCIAL AND ETHICS COMMITTEE REPORT .....	11

## OVERVIEW

South African company law and regulatory requirements determine the proposals which need to be presented to shareholders for approval. Of particular importance are the Companies Act 2008 (referred to as "CA" throughout this document), the Johannesburg Stock Exchange (JSE) Listings Requirements (referred to as "LR") and the King Code and Report on Governance for South Africa 2009 ("King III").

Legal and regulatory requirements are typically enshrined in a company's memorandum of incorporation ("MOI"), which is the constitutional document covering the governance of the company.

At the typical AGM, shareholders will be asked to approve the following:

- › Receipt of annual financial statements
- › Auditors' reappointment and remuneration
- › Election of directors
- › Election of audit committee members
- › Share issuance authorities
- › Share buyback authorities
- › Approval of director fees
- › Financial assistance to related or inter-related companies
- › Authority to ratify and execute approved resolutions
- › Approval of remuneration policy.

Non-routine items that are also often seen on South African agendas and require shareholder approval include:

- › Approval of new equity incentive schemes or amendments to existing schemes
- › Amendments to the MOI
- › Black Economic Empowerment (BEE) transactions
- › Social and ethics committee elections
- › Social and ethics committee report

Policies in this document are presented in an order consistent with a typical South African AGM agenda.

This document outlines the ISS policy on the above resolutions. For proposals which typically appear on an infrequent basis at South African meetings, and which are not covered in this document, ISS will refer to the EMEA Regional Policy as a framework for analysis.

## 1. ANNUAL FINANCIAL STATEMENTS

### *Local requirements*

Companies must submit their annual financial statements, including the reports of the auditors and the directors, to shareholders (CA s30). Although a large majority of South African companies submit their annual financial statements to a shareholder vote, this is not mandated by law. Some companies simply present the statements to the AGM without a formal vote. The JSE requires that annual financial statements and the AGM notice are sent to shareholders at least 15 business days before the AGM (LR s3.19).

▶ **General Recommendation:** Vote for approval of the financial statements and director and auditor reports, unless:

- › There are concerns about the accounts presented or audit procedures used; or
- › The company is not responsive to shareholder questions about specific items that should be disclosed publicly.

## 2. AUDITORS' REAPPOINTMENT AND REMUNERATION

### *Local requirements*

A public company must appoint an auditor at each AGM (CA s90). The retiring auditor can be automatically reappointed without any resolution being passed, but most companies include an appropriate agenda item. Some companies also seek separate shareholder approval for the remuneration paid to the auditors.

▶ **General Recommendation:** Vote for the re-election of auditors and/or proposals regarding auditor remuneration, unless:

- › There are serious concerns about the accounts presented or the audit procedures used;
- › The auditors are being changed without explanation; or
- › Non-audit related fees are substantial or are routinely in excess of standard audit-related fees.

## 3. DIRECTOR ELECTIONS

### *Local requirements*

The appointment of a new director must be confirmed by shareholders at the next AGM (LR schedule 10, para 10.16(c)). Furthermore, at least one-third of non-executive directors (NEDs) must retire by rotation at each AGM (LR schedule 10, para 10.16(g)), although at some companies retirement by rotation provisions extend to executive directors. Each director must be categorised as either executive, non-executive or independent (LR s3.84(f)).

▶ **General Recommendation:** Vote for the re-election of directors, unless:

- › Adequate disclosure has not been provided in a timely manner;
- › There are clear concerns over questionable finances or restatements, questionable transactions with conflicts of interest or records of abuses against minority shareholder interests;
- › The board fails to meet minimum governance standards;
- › There are specific concerns about the individual nominee, such as criminal wrongdoing or breach of fiduciary responsibilities;

- › Repeated absences (less than 75 percent attendance) at board and committee meetings have not been explained;
- › Elections are bundled;
- › The director is an executive who serves on one of the key board committees (audit, remuneration, nominations);
- › The director combines the roles of chairman and CEO and the company has not provided an adequate explanation;
- › The director is a former CEO who has been appointed as chairman;
- › The director is a non-independent NED who serves on the audit committee (unless there is a separate AGM proposal specifically covering his/her election as an audit committee member);
- › The director is a non-independent NED who serves on the remuneration or nomination committee and there is no majority of independent NEDs on the committee. However, such a consideration should take into account the potential implications for the board's Black Economic Empowerment (BEE) credentials;
- › The director is a non-independent NED and the majority of NEDs on the board are not independent. However, such a consideration should take into account the potential implications for the board's BEE credentials; or
- › Under extraordinary circumstances, there is evidence of egregious actions related to the director's service on other boards that raise substantial doubts about his or her ability to effectively oversee management and serve the best interests of shareholders at any company.

Proposals to re-elect alternate directors will take into account the vote recommendation that applies for the director for whom they serve as an alternate. In addition, the specific nature of the alternate role will be considered, for example whether or not the individual serves as a genuine alternate (i.e. only attending board and committee meetings in the absence of a particular director) or appears to have a broader board position.

### ISS Classification of Non-Independent Non-Executive Directors


#### Non-Independent Non-Executive Director (NED)

- › Any director who is attested by the board to be a non-independent NED;
- › Any director specifically designated as a representative of a significant shareholder of the company;
- › Any director who is also an employee or executive of a significant shareholder of the company;
- › Beneficial owner (direct or indirect) of at least 5 percent of the company's shares, either in economic terms or in voting rights;
- › Government representative;
- › Currently provides (or a related person provides) professional services to the company, to an affiliate of the company, or to an individual officer of the company or of one of its affiliates in excess of ZAR 100,000 per year. In line with King III, there should be a three-year cooling-off period for individuals appointed as the designated auditor/partner in the external audit firm or as a senior legal adviser to the company;
- › Represents customer, supplier, creditor, banker, or other entity with which company maintains transactional/commercial relationship (unless company discloses information to apply a materiality test, which indicates materiality if the company makes or receives annual payments exceeding the greater of ZAR 2 million or 5 percent of the recipient's gross revenues);
- › Any director who has cross-directorships with executive directors of the company;
- › Relative (immediate family member) of current or former executive of the company or its affiliates. King III specifies a three-year cooling-off period;
- › A new appointee elected other than by a formal process through the general meeting (such as a contractual appointment by a substantial shareholder);
- › Founder/co-founder/member of founding family but not currently an employee;
- › Former executive (five-year cooling off period); or
- › Any director who receives any form of performance-related remuneration.

## 4. AUDIT COMMITTEE ELECTIONS

### *Local requirements*

Companies (other than those covered by the Banks Act) must establish an audit committee of at least three members, which must be elected by shareholders at the AGM (CA s94).

 **General Recommendation:** Vote for the re-election of the audit committee and/or audit committee members, unless:


- › Committee member elections are bundled into a single voting item, and the committee includes one or more non-independent NEDs;
- › Committee members are elected individually, and the audit committee member is a non-independent NED;
- › Repeated absences (less than 75 percent attendance) at committee meetings have not been explained; or
- › There are serious concerns about the accounts presented, the audit procedures used, or some other feature for which the audit committee has responsibility.

## 5. SHARE ISSUANCE AUTHORITIES

### *Local requirements*

In line with the provisions of its MOI, a company will typically seek a general authority to issue shares (sometimes referred to as "placing shares under the control of the directors"). This authority can be used to issue shares on a non-preemptive basis. The JSE has separate rules governing the issue of shares for cash. The Listings Requirements allow companies to request a general authority to issue shares for cash up to a maximum of 15 percent of the issued share capital on a non-preemptive basis, subject to approval by shareholders (LR s3.32, s5.52). The JSE specifies that a general authority to issue shares for cash requires 75 percent support.

Preference shares are reasonably common in South Africa, and some companies routinely seek separate authorities to issue new preference shares.

 **General Recommendation:** Vote for a general authority to place authorised but unissued ordinary shares under the control of the directors, unless:

- › The authority is over a number of shares equivalent to more than 10 percent of the current issued share capital;
- › The authority would allow shares to be used for share incentive scheme purposes and the underlying scheme(s) raises concern; or
- › The company used the authority during the previous year in a manner deemed not to be in shareholders' best interests.

Vote for a general authority to issue ordinary shares for cash, unless:

- › The authority is over a number of shares equivalent to more than 10 percent of the current issued share capital; or
- › The company used the authority during the previous year in a manner deemed not to be in shareholders' interests.

Vote for a general authority to issue preference shares, unless:

- › Following the issue, preference shares would comprise greater than 50 percent of the company's issued share capital; or


- › The terms of the preference shares would adversely affect the rights of existing shareholders.

The issue of shares pursuant to a specific transaction will be considered on a case-by-case basis, depending on the merits of the underlying deal.

## 6. SHARE BUYBACK AUTHORITIES

### *Local requirements*

Companies are allowed to acquire their own shares (CA s48). The JSE specifies a number of conditions in relation to share buybacks, one of which is that general authorities are permitted up to 20 percent of the issued share capital in any one financial year (LR s5.68). Further, general authorities require the approval of shareholders by way of a special resolution (LR s5.72).


 **General Recommendation:** Vote for a general share buyback authority, unless:

- › The company wishes to repurchase more than 20 percent of its issued share capital over the year;
- › The repurchase can be used for takeover defenses; or
- › There is clear evidence of abuse.

## 7. FEES FOR NON-EXECUTIVE DIRECTORS

### *Local requirements*

The remuneration paid to directors for their services as directors can only be paid in accordance with a special resolution approved by shareholders within the previous two years (CA s66). (This relates to the fees payable to directors, not the remuneration which an executive director will receive as an employee of the company, and therefore in practice concerns the fees paid to non-executives.) Companies either seek approval for these fees under one resolution, or provide separate resolutions for each different type of fee.


 **General Recommendation:** Vote for the fees payable to non-executive directors, unless:

- › The proposed fees are excessive, relative to similarly-sized companies in the same sector.

## 8. FINANCIAL ASSISTANCE TO RELATED OR INTER-RELATED COMPANIES

### *Local requirements*

Under the Companies Act, companies are required to seek shareholder approval in advance of providing certain forms of financial assistance (e.g. loans or loan guarantees) (CA s44, s45). Approval is required for assistance provided to (a) related or inter-related companies (e.g. a subsidiary), (b) directors or prescribed officers (i.e. senior executives who are not directors), (c) for the purpose of subscribing for any options or securities issued by the company or by a related or inter-related company, or (d) for the purpose of purchasing any securities of the company or a related or inter-related company.

 **General Recommendation:** Vote for a general authority to provide financial assistance, unless:

- › As part of the authority, the company requests a general authority to provide financial assistance to directors, and this is not limited to participation in share incentive schemes; and/or
- › As part of the authority, the company seeks approval to provide financial assistance "to any person."

Evidence that the company has used a previous authority in a manner deemed not to be in shareholders' interests would warrant further review and analysis.

## 9. AUTHORITY TO RATIFY AND EXECUTE APPROVED RESOLUTIONS

### *Local requirements*

Many companies seek the approval of shareholders for a formal authority allowing the directors (and/or the company secretary) to sign all the necessary documents and do everything required to put into effect the resolutions approved at the general meeting.


 **General Recommendation:** Vote for the authority to ratify and execute approved resolutions, unless:

- › Opposition is recommended to all other items on the agenda.

## 10. APPROVAL OF REMUNERATION POLICY

### *Local requirements*

The King III report recommends that companies provide shareholders with an annual non-binding vote on the remuneration policy (principle 2.27). The vote has advisory status in respect of the remuneration policy and specific pay packages.

 **General Recommendation:** ISS evaluates management proposals seeking ratification of a company's remuneration policy on a case-by-case basis. When judging remuneration policies, ISS generally recommends a vote against if the



level of disclosure of the policy and/or its application is below what is required for shareholders to make an informed judgment on the policy. In the event of satisfactory disclosure, ISS recommends a vote for the approval of the executive remuneration policy unless TWO or more of the following issues apply (NB it may be appropriate to vote against on ONE issue if it has been identified as particularly serious):

- › Large increases in fixed remuneration have been implemented which have not been adequately explained.
- › The company has made bonus payments but these have not been clearly linked to performance (including guaranteed bonuses or transaction bonuses).
- › The company operates long-term incentive schemes (including matching shares) which do not have performance conditions attached for all or a substantial proportion of awards, or if performance conditions are in place, they are not disclosed or are not considered sufficiently challenging or relevant.
- › The vesting period for long-term incentive schemes is set at less than three years.
- › Long-term schemes include an element of retesting.
- › Options can be granted at a discount to market value.
- › The potential maximum dilution under all share incentive schemes exceeds 5 percent of the issued share capital of a large, widely held company, or 10 percent in the case of an emerging high-growth company, and there are no mitigating circumstances (e.g. stringent performance measures).
- › The company has made ex-gratia payments or one-off special awards to executives during the year which have not been adequately explained.
- › Discretion has been used during the year in a manner not considered consistent with shareholder interests.
- › The policy or the application of the policy is in any way not considered aligned with shareholder interests.

In circumstances where a company has demonstrated a significant shift in the right direction, it may be appropriate for ISS to support the remuneration policy resolution, notwithstanding the presence of some historical issues of concern.

Failure to propose a resolution on executive remuneration for shareholder approval may lead to an adverse vote recommendation on another AGM item, for example the re-election of the chairman of the remuneration committee.

## 11. NEW EQUITY INCENTIVE SCHEME OR AMENDMENT TO EXISTING SCHEMES

### **Local requirements**

Share incentive schemes which involve the issue of new shares must be approved by shareholders via a resolution requiring 75 percent support (LR schedule 14). Certain provisions in existing schemes cannot be altered without shareholder approval.

**General Recommendation:** ISS evaluates management proposals seeking approval for a share incentive scheme on a case-by-case basis. When judging such items, ISS will generally recommend a vote against if the level of disclosure on the proposal is below what is required for shareholders to make an informed judgment on the scheme. In the event of satisfactory disclosure, ISS will recommend a vote for the proposal unless ONE or more of the following apply:

- › Performance conditions do not apply, have not been disclosed or are not considered sufficiently challenging or relevant.
- › Performance conditions can be retested.
- › Performance is measured over a period shorter than three years.
- › The plan allows for option repricing or issue of options at a discount or backdating of options.

- › The potential maximum dilution under all share incentive schemes exceeds 5 percent of the issued share capital of a large, widely held company, or 10 percent in the case of an emerging high-growth company, and there are no mitigating circumstances (e.g. stringent performance measures).
- › The scheme provides for potentially excessive individual reward or has no caps on individual participation.
- › NEDs can participate in the scheme.
- › The scheme is in any way not considered aligned with shareholder interests.

Proposals to amend a scheme will involve an assessment of the nature of the amendment.

## 12. NEW MEMORANDUM OF INCORPORATION (MOI)/AMENDMENTS TO THE MOI

### *Local requirements*

Shareholder approval is required for a new MOI or amendments to the existing MOI (CA s16). The Listings Requirements include detailed guidance on what should be included within an MOI (schedule 10).

- ▶ **General Recommendation:** Vote on a new MOI or on amendments to the MOI on a case-by-case basis, depending on the impact on shareholder rights.

ISS will normally recommend a vote against an MOI which limits retirement by rotation to non-executive directors only.

## 13. BLACK ECONOMIC EMPOWERMENT (BEE) TRANSACTIONS

### *Local requirements*

BEE transactions often involve the issue of new shares to specific partners or the provision of financial assistance and, as such, require shareholder approval. The precise nature of the transaction can vary significantly from company to company.

- ▶ **General Recommendation:** Vote on BEE transactions on a case-by-case basis. Factors considered include the overall dilutive impact, the structure of the transaction and the identity of the company's chosen BEE partners. Proposals which are genuinely broad-based are more appealing than those which stand to benefit a narrow group of investors, as are those which have a long-term timeframe.

## 14. SOCIAL AND ETHICS COMMITTEE ELECTIONS

### *Local requirements*

The Companies Act includes provisions envisaging that companies form a social and ethics committee (CA s72). Further legislation – in the form of the Companies Regulations 2011 – specifies that these committees must include at least three directors or prescribed officers, at least one of whom must be a director who is not involved in day-to-day management (s43). There is no requirement for shareholders to vote on the members of the committee, but a small minority of companies include these elections on the AGM agenda.

▶ **General Recommendation:** Vote for the re-election of the social and ethics committee and/or social and ethics committee members, unless:

- › The committee does not satisfy the minimum guidelines for membership, as set out in South African company law; or
- › Serious concerns have been raised with the work of the committee during the year.

## 15. SOCIAL AND ETHICS COMMITTEE REPORT

### *Local requirements*

The Companies Regulations 2011 require the social and ethics committee to report, through one of its members, to the shareholders at the AGM on the matters within its mandate (s 43). There is no requirement for shareholders to vote on this report, but a small minority of companies include this as a voting item on the AGM agenda.

▶ **General Recommendation:** Vote for the report of the social and ethics committee, unless:

- › The report does not include details of how the committee has undertaken the functions prescribed to it by South African company law; or
- › Serious concerns have been raised with the work of the committee during the year.

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