

# LongView Funds Domestic Proxy Voting Guidelines

Re-affirmed 27 March 2014

## Preamble

### LongView General Principles on Corporate Governance

Amalgamated Bank's LongView Collective Investment Funds (the "Funds") were established in 1992 with the objective of delivering sustainable investment returns while promoting long-term shareholder value by actively voting each proxy according to the highest standards of corporate governance and engaging portfolio companies to advocate corporate policies and practices in the interests of long-term shareholder value. The Funds' proxy voting and engagements with companies are driven by key principles that the Funds believe define good governance and enhance the prospects for sound shareholder returns.

- **Shareholder Democracy:** The Funds espouse the principle of "one-share, one-vote." Shareholders should be treated equally and fairly, and governance structures and voting systems should enable reasonable participation of the firms' owners, the shareholders.
- **Accountability:** Board election standards and practices should ensure that board members are accountable to shareholders. Boards are responsible for setting overall strategy. In turn, management is responsible for implementing such strategy and is accountable to the board. Management's goals and objectives should be appropriately aligned and regularly reviewed.
- **Prudent Risk Oversight:** Boards and management teams should develop corporate practices that are viable over the long-term and minimize the risks of potential costs, damages, and other liabilities from legal, regulatory, operational, and reputational risks inherent in the business.
- **Social and Environmental Awareness:** Companies should minimize negative externalities. Short-term business practices (e.g. pollution) might generate long-term risks for a company (e.g. legal, regulatory, operational, and reputational) and impose costs elsewhere in our economy, thereby undermining the interests of long-term investors.
- **Alignment of Compensation Practices with Sustainable Value Creation:** Executive compensation should be aligned with long-term firm performance and create appropriate incentives for sustainable, long-term growth.

The Funds believe that sound governance practices promote a stable investment climate, that is advantageous for all investors. Towards that end, the Funds actively collaborate with other key institutional investors. The Funds are active participants in the Council of Institutional Investors, a coalition of public, labor, and corporate pension funds representing over \$4 trillion in assets under management. The Funds are affiliated with the International Corporate Governance Network, the Investor Network on Climate Risk, and the Interfaith Center on Corporate Responsibility. The Funds are also a founding signatory (2006) of the United Nations Principles for Responsible Investment (UN PRI), an international network of investors representing over \$18 trillion in assets in 36 different countries, all committed to pursuing improved environmental, social, and governance (ESG) compliance in international markets.

## LongView Process for Voting Proxies

The Funds are sponsored by the Amalgamated Bank as vehicles for tax-exempt investors to invest assets in publicly listed equities. The Amalgamated Bank, as Trustee for the Funds, is responsible for voting the Funds' proxies for the annual and special meetings held by these companies.

The LongView Funds Domestic Proxy Voting Guidelines (the "Guidelines") constitute the foundation for the administration and rationale for voting proxies at portfolio companies on behalf of the Funds. The Guidelines contain certain policies and parameters for the voting of proxies with respect to the shares owned by the Funds. The Guidelines are designed to promote corporate policies and practices that the Funds believe will enhance shareholder value and are in their long-term interests as shareholders.

The Amalgamated Bank has adopted the Guidelines for the purpose of setting forth the Funds' policies with respect to frequently proposed proxy voting issues concerning environmental, social, and governance matters. Where the Guidelines call for CASE-BY-CASE analysis of a voting item, where the Guidelines are silent on a proxy item to be voted, or where a proxy voting issue is sufficiently complex or sensitive, the Amalgamated Bank receives an analysis and report from proxy advisory research services in order to inform how to vote in line with the general principles and philosophies as outlined in the Preamble, defined in the following Guidelines, and any specific relevant factors. The Amalgamated Bank may consult with additional information services, industry or equity analysts, and additional data sources in order to administer the Funds' vote in accordance with the Funds' long-term interests in shareholder value at the portfolio company.

## Table of Contents

<b>1. Board of Directors</b>	<b>1</b>
1.1 Election of Directors	
1.1a Uncontested Election of Directors	
1.1b Contested Elections or Proxy Contests	
1.2 Board Composition	
1.2a Annual Election of Directors	
1.2b Majority Vote Standard for Director Elections	
1.2c Size of the Board	
1.2d Term Limits	
1.2e Board Diversity	
1.3 Board Leadership	
1.3a Establish Independent Board Chair	
1.3b Separate Board Chair and Chief Executive Officer	
1.3c Establish Lead Independent Director	
1.4 Independent Committees	
1.4a Independent Audit Committee	
1.4b Independent Nominating Committee	
1.4c Independent Compensation Committee	
1.5 Shareholder Access to the Proxy	
1.6 Shareholder Advisory Committee	
1.7 Limiting Director Liability	
1.8 Indemnification	
<b>2. Auditors</b>	<b>5</b>
2.1 Proposals to Ratify Selection of Auditor	
2.2 Proposals to Require Shareholders to Ratify Selection of Auditor	
<b>3. Capital Structure, Mergers &amp; Acquisitions, and Shareholder Rights</b>	<b>6</b>
3.1 Stock Authorizations	
3.1a Increasing Authorized Common Stock	
3.1b Blank Check Preferred Stock	
3.2 Shareholder Approval of Targeted Share Placement	
3.3 Dual Class Voting Structures	
3.4 Shareholder Rights Plan or Poison Pills	
3.4a Proposals to Approve Poison Pills	
3.4b Proposals to Redeem Poison Pills	
3.4c Proposals Seeking Shareholder Approval of Poison Pills	
3.5 Restrict Payment of Greenmail	
3.6 Opt Out of Delaware's Anti-Takeover Law	
3.7 Supermajority Voting Requirements	
3.8 Preemptive Rights	
3.9 Mergers, Sales, Acquisitions and Other Business Combinations and Reorganizations	
3.10 Fair Price Provisions	
3.11 Confidential Voting	

3.12	Cumulative voting	
3.13	Shareholder Right to Act by Written Consent	
3.14	Shareholder Right to Call a Special Meeting	
3.15	Reincorporation	
3.16	Judicial Forum or Venue	
<b>4.</b>	<b>Executive Compensation</b>	<b>13</b>
4.1	Advisory Vote on Executive Compensation	
4.1a	Shareholder Proposals Calling for Advisory Votes on Executive Compensation	
4.1b	Advisory Votes on Executive Compensation	
4.1c	Frequency of Advisory Votes on Executive Compensation	
4.2	Equity and Incentive Compensation Plans	
4.3	Pay-for-Performance	
4.4	Disclosure of Integrating Executive Compensation with Sustainability Risks	
4.5	Severance Agreements and Golden Parachutes	
4.5a	Proposals to Obtain Shareholder Approval for Parachutes	
4.5b	Proposals to Approve Severance Payments in Connection with a Merger or Acquisition	
4.5c	Proposals to Prohibit Commitments to Pay Excise Tax “Gross-Ups”	
4.5d	Proposals to Prohibit Accelerated Vesting of Unearned Equity	
4.6	Clawbacks and Recoupment Policies	
4.7	Restrictions on Executive Compensation	
4.8	Non-Executive Director Compensation	
4.8a	Proposals to Grant Equity or Awards to Non-Employee Directors	
4.8b	Prohibit Extending Retirement Benefits to Non-Executive Directors	
4.9	Equity Ownership for Executives and Directors	
4.10	Prohibit Insider Trading	
4.11	Responsible Use of Company Stock	
4.12	Employee Share Ownership Plans	
<b>5.</b>	<b>Environmental and Social Issues</b>	<b>19</b>
5.1	Environmental Issues and the CERES Principles	
5.1a	Proposals Requesting Commitment to Support CERES Principles	
5.1b	Proposals Requesting Public Reporting on Environmental Practices	
5.2	Political Contributions Disclosure	
5.3	Charitable Contributions	
5.4	Equal Employment Opportunity	
5.5	High-Performance Workplaces	
5.6	Human Rights and Codes of Conduct	
5.7	Corporate Activity in Northern Ireland – The MacBride Principles	
5.8	Health Care Policy	
5.9	Access to Medicine	
5.10	Tobacco Advertising and Production	
5.11	Animal Protection	
	<b>Appendix A: Council of Institutional Investors Definition of Director Independence</b>	<b>22</b>
	<b>Appendix B: Equity and Incentive Compensation Plan Definitions</b>	<b>24</b>
	<b>Appendix C: The CERES Principles</b>	<b>28</b>
	<b>Appendix D: The MacBride Principles</b>	<b>30</b>

## 1. Board of Directors

### 1.1 Election of Directors

#### 1.1a Uncontested Election of Directors: CASE-BY-CASE ANALYSIS

The board of directors of a company formulates corporate policies and monitors the activities of management in implementing those policies. The election of the members of a board of directors is one of the few opportunities that the shareholders of a company have to determine the manner in which the company is governed.

In determining to vote “for” or “against” (or “withhold”) from individual director nominees, the LongView Funds will consider the following factors:

**(a) Independence:** In order to properly exercise independent oversight on behalf of shareholders, the Funds believe that at least two-thirds of the board should be comprised of independent directors. The Funds may vote against one or more of the non-independent directors if the board does not have a two-thirds majority of independent directors. The Funds’ definition of an independent director is substantially the same as the definition used by the Council of Institutional Investors, found within Appendix A. The Funds consider a director to be “independent” if he or she: (i) is not currently employed by the company or any of its affiliates and has not been employed by the company or an affiliate in an executive capacity within the last five years; (ii) is not a member of a corporation, partnership, firm, or other entity that is one of the company’s paid advisors or consultants (such as the company’s legal counsel or investment banker); (iii) is not employed by a significant customer or supplier of the company and is not a significant debtor to or creditor of the company (A significant customer or supplier of the company is one that has sales to or by the company that represent more than 1% of the sales of the customer or supplier or more than 1% of the sales of the company. A significant debtor or creditor of the company is one that owes to the company or is owed by the company an amount that exceeds 1% of the company’s or the third party’s assets); (iv) has no personal services contract with the company; (v) is not employed by a foundation or university that receives significant grants or endowments from the company; (vi) is not a relative of a member of the management of the company; and (vii) is not part of an interlocking directorate, whereby the chief executive officer or other executive officer of the company serves on the board of directors of another corporation that employs the director.

**(b) Company Performance:** The Funds may compare the company’s performance to the performance of a relevant equity index or to the performance of the company’s peer group. In general, if the company’s short-term and long-term financial performance (measured by total shareholder return) over the previous five years has substantially underperformed these benchmarks, the Funds may vote against all nominees to the board.

**(c) Attendance:** The Funds will vote against any nominee who is a director of the company and has failed to attend at least 75% of the meetings of the board of directors during the last fiscal year and the proxy statement does not provide a reasonable explanation for such individual’s absences.

**(d) Executive Compensation:** The Funds may consider whether the total compensation paid to the chief executive officer of the company and the other four most highly paid executive officers is reasonable in view of the company's performance. (Under the Securities and Exchange Commission rules, disclosure of compensation paid to officers is only required in a company's proxy statement with respect to the chief executive officers and the four other most highly compensated executive officers.)

**(e) Antitakeover Defenses:** The Funds may consider whether the antitakeover defenses (if any) adopted by a company are reasonable.

**(f) Conflicts of Interest:** The Funds may vote against any nominee who has a significant conflict of interest in serving as director of the company. For example, if the nominee receives consulting fees from the company and such fees are unusual in nature or amount, or if a nominee owns a significant equity interest in or is a principal manager of a business organization to which the company made or from which it received commercial payments, the Funds may consider a vote against such nominee.

**(g) Shareholder Responsiveness:** The Funds may vote against the entire Board if the Board has failed to implement proposals that have been supported by the majority of votes cast.

**(h) Overboarding:** The Funds may vote against a nominee who serves on an excessive number of public company Boards (three other boards for full-time working managers, five other boards for others) which may jeopardize the nominee's ability to perform the requisite duties as a director.

**(i) Performance on Other Boards:** The Funds may vote against or withhold votes from a nominee who has served as a director of a public company with an egregious record of poor performance (e.g., withhold votes for trustees on Enron's board).

**(j) Insiders Serving on Key Board Committees:** The Funds will vote against or withhold votes from nonindependent nominees serving on audit, compensation, or nomination committees.

**(k) Other Factors:** The Funds may analyze business decisions previously made by the directors and the ability of current management to address and rectify company problems.

#### **1.1b Contested Elections or Proxy Contests: CASE-BY-CASE ANALYSIS**

The Funds will vote each nominee in contested elections upon examination of the company's long-run performance, current management's ability to rectify any problems, the personal qualifications of the opposing slate, and the anticipated economic impact of the policies that they advance.

### **1.2 Board Composition**

#### **1.2a Annual Director Elections: FOR**

The Funds favor annual elections and believe that annual elections for directors promote accountability by allowing shareholders to review director performance and determine a vote for every director each year. Classified boards, or staggered boards (by which directors are divided into three "classes" and elected only once every three years) limit shareholders' ability to register support or opposition to director performance. Classified boards also may discourage takeovers and thereby reduce potential receipt by shareholders of a takeover premium.

**1.2b Majority Vote Standard for Director Elections: FOR**

The Funds believe that, in uncontested elections, a director should be elected by a majority of the votes cast. Under a majority vote standard, a director nominee must receive the support of “50% plus one” of the votes cast in order to be elected. Majority vote standards promote shareholder democracy by ensuring that directors are elected with the support of a majority of voting shareholders. Under most state corporate laws, including Delaware’s statutes, a plurality vote is the default standard in the election of the board of directors. Under the plurality vote standard, a director nominee in a director election can be elected or re-elected with as little as a single affirmative vote, even if a substantial majority of the votes cast are withheld from that director nominee. In contested elections, or “proxy contests,” in which there are more nominees than available board positions, the Funds support the application of a plurality vote standard.

**1.2c Size of the Board: CASE-BY-CASE ANALYSIS**

The Funds generally approve of modifications to the size of the board if the proxy statement provides a satisfactory rationale. An explanation is not satisfactory if the intent is to add new directors who support unreasonable takeover defenses or other policies inconsistent with the views expressed in these Guidelines.

**1.2d Term Limits: AGAINST**

The Funds generally oppose proposals to impose term limits on director tenure. The Funds believe that term limits may serve as an overly rigid restriction and make ineligible for re-election directors who through their years of service have acquired substantial knowledge of the company’s business and operations that are beneficial to shareholders.

**1.2e Board Diversity: FOR**

The Funds generally support reasonable proposals requesting that companies adopt policies or recruit board nominees from diverse populations which may add to the diversity of perspectives on the board and benefit shareholder value. Board diversity may address broader participation on the board by women, people of color, company employees, or key stakeholder communities for the company.

**1.3 Board Leadership**

The task of the board of directors is to protect shareholders’ interests by providing independent oversight of management, including the chief executive officer. As a general matter, the Funds believe that having a board chair who is independent of the company and its management is a governance practice that will promote greater board accountability to shareholders and lead to a more objective evaluation and oversight of management. The Funds accordingly believe that, whenever possible, the chair of the board of directors should be an independent director, as defined by the Council of Institutional Investors (see Appendix A), and who has not previously served as an executive officer of the company.

**1.3a Establish Independent Board Chair: FOR**

The Funds generally vote for proposals to establish independent board chairs.

**1.3b Separate Board Chair and Chief Executive Officer: FOR**

The Funds generally support proposals to separate the roles of board chair and chief executive officer.

**1.3c Establish Lead Independent Director: FOR**

At companies at which one individual serves both roles of chair and chief executive officer, the Funds generally support the establishment of a lead independent director.



#### **1.4 Independent Committees**

The Funds believe that key committees of the board should be comprised of independent directors. Various stock exchanges and laws require key board committees to be comprised of independent directors, although some provisions allow for exemptions for certain companies. The Funds support strong independent committees for all companies across the Funds' portfolios. The Funds use a definition of independence similar to that established by the Council of Institutional Investors (see Appendix A).

##### **1.4a Independent Audit Committee: FOR**

The Funds believe that the oversight of companies' financial integrity should not be the responsibility of those with personal stakes in favorable reviews. Directors who are independent of management are best qualified to exercise their responsibilities in the interests of shareholders.

##### **1.4b Independent Nominating Committee: FOR**

A nominating committee of the board of directors usually is responsible for recruiting and recommending new directors to the company's board of directors. The Funds believe that an independent nominating committee makes the board more accountable to shareholders and may increase shareholder participation in and influence over director selection.

##### **1.4c Independent Compensation Committee: FOR**

The compensation committee is responsible for the oversight of compensation policies for senior executives. The Funds believe that directors independent of management are best qualified to act in the interests of the shareholders, avoid conflicts of interest, and take steps necessary to evaluate management performance and establish a suitable alignment between company performance and executive compensation levels and policies.

#### **1.5 Shareholder Access to the Proxy: FOR**

The Funds believe that shareholders should have reasonable options to nominate director candidates of their choosing to the corporate proxy, also known as "proxy access." Proxy access promotes shareholder democracy and enables shareholders to be able to select the most appropriate director candidates to best represent their interests. The Funds therefore support reasonable proposals that facilitate the ability of a shareholder or shareholders who own a reasonable minimum threshold of voting shares to nominate a director or group of directors to the proxy for voting consideration by fellow shareholders.

#### **1.6 Shareholder Advisory Committee: CASE-BY-CASE ANALYSIS**

A shareholder advisory committee is a group of shareholders designated to provide advice to the board of directors regarding the interests of shareholders on company policy concerning a variety of matters. The Funds generally support reasonable proposals to create a shareholder advisory committee because they believe that such committees allow company actions to be taken with greater consideration of the views of the shareholders and that the decision-making of a company is improved by enhancing shareholder influence on company policy. Reasonable proposals require such committees to provide non-binding advice. The committee may provide shareholder perspective on a variety of topics relevant to the company and its business (such as major restructurings or acquisitions, mergers, and compensation issues) and other matters on which the board may choose to consult the committee. The Funds may oppose proposals to create advisory committees if the proposed committee would be cumbersome and excessively costly for the company to maintain.

### **1.7 Limiting Director Liability: FOR**

Proposals typically call for shareholders to vote to adopt an amendment to the company's charter to eliminate or limit the personal liability of directors to the company and its shareholders for monetary damages for any breach of fiduciary duty to the fullest extent permitted by the laws of the state in which the company is incorporated. The Funds generally support proposals to limit director liability, provided that limitations do not apply to illegal insider dealing; breach of duty of loyalty; intentional misconduct; or paying illegal dividends or approving illegal stock purchases. The Funds believe that some limitations on directors' liability are necessary in order to attract and retain competent individuals to serve as directors.

### **1.8 Indemnification: FOR**

Indemnification is the payment by a company of costs and expenses incurred by covered individuals who become defendants in a lawsuit as a result of their corporate affiliations. Indemnification can cover expenses as well as amounts paid to settle lawsuits or to satisfy judgments rendered against the individual defendants. Proposals to indemnify a company's directors differ from proposals to limit or eliminate directors' liability in that with indemnification the individual covered by indemnification may still be liable for an act or omission, but the company agrees to pay damages assessed as a result of such liability. Shareholder approval of most indemnification provisions and indemnification agreements is not required by law, although many companies submit them to shareholder votes because of the potential conflict of interest for the directors who approve the provisions or agreements and also benefit from them.

Proposals usually call for the shareholders to approve indemnification provisions, increase the level of indemnification provided by the company, or approve indemnification agreements between the company and its directors and/or officers. The Funds generally support indemnification proposals, except in instances where they provide protection beyond that allowed under state law or seek to insulate directors from liability for actions already taken. The Funds believe that companies cannot attract and retain qualified individuals to serve as directors and officers without offering them protection from personal liability for their good faith decisions. The Funds do not believe it is appropriate, however, to approve indemnification provisions shielding directors from liability for actions already taken.

## **2. Auditors**

Auditors are independent accountants who review a company's financial records to ensure that the company is accurately reporting its financial condition to the public. The independent auditors assess the quality of the financial reports prepared by the company and issue an opinion with respect to the company's accounting information. The audit committee of a board of directors generally is responsible for recommending the independent auditor. Companies are not required to have shareholders approve their selection of an outside auditing firm, although most companies do ask shareholders to ratify their choice. Such approval usually is considered a routine voting matter.

### **2.1 Proposals to Ratify Selection of Auditor: CASE-BY-CASE ANALYSIS**

Management proposals call for the shareholders to ratify the board of directors' selection of an auditor. The Funds support the board's recommendation on the selection of a company's independent auditor unless there are unusual circumstances present that would cause the Funds to oppose the board's selection. Such unusual circumstance may include a material conflict of interest, financial problems with the company that the auditor failed to notice, or the company has changed or proposes to change auditors following an unfavorable opinion rendered by the previous auditor.

## **2.2 Proposals to Require Shareholders to Ratify Selection of Auditor: FOR**

The Funds support the right of shareholders to approve of, or object to, the board of directors' selection of an auditor. Although in most cases the selection of a company's auditors is a routine business matter, a regular ratification process encourages accountability from auditors and enables shareholders to object when circumstances merit a vote against.

# **3. Capital Structure, Mergers & Acquisitions, and Shareholder Rights**

## **3.1 Stock Authorizations**

### **3.1a Increasing Authorized Common Stock: CASE-BY-CASE ANALYSIS**

A company's charter must specify the number of shares of common stock that the company is authorized to issue. In order to increase the number of authorized shares, it is necessary to amend the company's charter, which requires shareholder approval. Management may request that shareholders approve a charter amendment that authorizes additional common stock for a number of reasons including to implement a stock split, to effect a restructuring or acquisition, or to provide sufficient shares for issuance under a stock option, stock purchase, or other similar plan. Management also may seek to increase the company's authorized shares in order to implement a "poison pill" or other antitakeover defense.

The Funds will support proposals to authorize additional common stock if management provides satisfactory business reasons for the increase. Satisfactory reasons for authorizing additional common stock generally include stock splits, stock dividends, stock option plans, and additional financing needs. When, however, management fails to disclose valid, specific business reasons for the proposed increase in authorized common stock, seeks shares in excess of what is reasonably necessary for the valid business reasons disclosed, or proposes an increase in the number of authorized shares in order to implement an antitakeover defense such as a poison pill not supported by the Funds, the Funds generally will not support the proposal.

### **3.1b Blank Check Preferred Stock: AGAINST**

Preferred stock of a company is stock that grants to the holders some preferential right to the company's earnings, assets, or both and may be either voting or nonvoting or may carry only contingent voting rights (for example, after a default in payment of preferred dividends). Blank check preferred stock is preferred stock that is authorized by a company's shareholders, but that gives the board of directors broad discretion to establish voting, dividend, and other rights and preferences when such stock is issued. Once this blank check stock is authorized, a company's shareholders have no further power to determine the terms of the stock or in most cases how or when it will be issued.

Blank check preferred stock often is used to effect a restructuring or acquisition. It also can be used as an antitakeover device. For example, management can place the stock into the hands of investors who would vote against a merger, sale of assets, or other corporate transaction. In addition, such stock can be used to implement a poison pill defense against a party who is attempting to gain control of a company without board approval. Further, if preferred stock is issued with multiple voting rights or is convertible into multiple shares of common stock, it may deter an interested party from tendering an offer to other shareholders for the company's common stock because the existence of such preferred stock may make the acquisition unacceptably expensive to the potential acquiror.

The Funds generally oppose management proposals to authorize blank check preferred stock, such as proposals to approve an amendment to the company's charter that allows the board of directors to issue preferred stock having such voting and other rights as the board, in its sole discretion, may determine. Generally, the risks outweigh the benefits because such a measure would allow company management to alter shareholder voting power, adopt poison pills, and take other actions without shareholder approval.

### **3.2 Shareholder Approval of Targeted Share Placement: FOR**

A targeted share placement is the sale by a company of a sizable block of shares to a friendly investor, such as employees or large corporate or institutional investors. The targeted placement of stock, particularly blank check preferred stock, can be used by management to deter unsolicited takeover bids by issuing a block of stock to a party that will vote with management in a proxy contest. The Funds support proposals to require shareholder approval of targeted share placements. By requiring shareholder approval prior to such placements, shareholders will be better able to ensure that a company's stock placement is not being used to deter an unsolicited tender offer that may be favorable to shareholders.

### **3.3 Dual Class Voting Structures: AGAINST**

Dual class voting proposals typically call for the issuance of new shares of stock with unequal voting rights. Dual class voting can normally be implemented only by means of a charter amendment. A company can establish dual class voting through an exchange offer, a stock dividend, a public offering of newly-issued stock, or some other recapitalization. The SEC and the stock exchanges all limit companies' ability to establish dual class voting by any of these means. Proponents argue that because dual class voting usually results in a control group maintaining substantial voting rights and the public receiving lesser rights, dual class voting vests control in a group with a substantial equity investment, which can coordinate decision-making and promote profitable activities. Opponents contend that dual class voting violates the one-share, one-vote principle and distorts corporate control by favoring certain shareholders' interests over others. Further, opponents note that giving an effective veto to a control group can serve as a takeover defense.

The Funds oppose dual class voting structures. The Funds believe that one-share, one-vote is a sound and fundamental principle of corporate governance. Dual class voting compromises this principle and, if accomplished through an exchange offer or other recapitalization, will either disenfranchise or dilute the voting power of existing shareholders. Moreover, the anti-takeover feature of dual class voting can discourage takeover bids that may benefit the Funds' investors. As a result of these problems, dual class voting can adversely affect share prices.

### **3.4 Shareholder Rights Plan or Poison Pills**

Shareholder rights plans, commonly referred to as "poison pills," are intended to provide protection to a company by reducing the risk that a hostile entity will be able to acquire control of the company through coercive acquisition techniques or for an inadequate price by making the acquisition unacceptably expensive to the potential acquiror. Under a typical plan, the company issues rights to its shareholders in the form of a dividend that entitles the shareholders to purchase stock in their own company (a "flip-in" plan) or in the acquiring company (a "flip-over" plan) at a significant discount (usually 50%) from the market price. (Most poison pills now contain both flip-over and flip-in provisions.) The rights are exercisable when a hostile third party acquires a certain percentage (generally between 10% and 30%) of the company's voting stock. If the rights are triggered and to the extent the rights are exercised, the "poison pill" would dilute the percentage ownership and the value of the acquiror's holdings, thereby effectively preventing the acquiror from acquiring control of the company.

The board of directors of a company that has adopted a rights plan retains the discretion to redeem the rights (at a nominal amount) in order to prevent the rights from interfering with a negotiated merger, management buy-out, or other friendly acquisition. Shareholder rights plans can be adopted by a board of directors without shareholder approval. Some companies, however, have submitted their plans to a shareholder vote in response to shareholder opposition to these plans or to strengthen the enforceability of a plan in the event it is later subject to challenge in a takeover situation. Proposals with respect to rights plans usually are made by shareholders. Shareholder proposals with respect to poison pills fall into three major categories, including: (i) proposals seeking shareholder approval of poison pills, (ii) proposals calling for redemption of the pill, and (iii) proposals asking for a binding shareholder vote on the pill.

### **3.4a Proposals to Approve Poison Pills: AGAINST**

The Funds generally oppose management proposals to approve adoption of a rights plan. Such plans serve to entrench management and may have a negative effect on share value. The Funds may consider supporting rights plans where plans are both narrowly designed and of limited duration to preserve preferable tax treatment for net operating losses (“NOLs”).

### **3.4b Proposals to Redeem Poison Pills: FOR**

The Funds generally support proposals to redeem a company’s existing rights plan that was originally adopted by the company without shareholder approval.

### **3.4c Proposals Seeking Shareholder Approval of Poison Pills: FOR**

The Funds support proposals to require the company to submit any proposed rights plan to a binding shareholder vote. Shareholders should approve corporate decisions, such as adoption of a rights plan, that could have a material effect upon the company and its shareholders.

### **3.5 Restrict Payment of Greenmail: FOR**

The payment of “greenmail” refers to when a company that is the target of a hostile takeover bid attempts to prevent the takeover by agreeing to purchase the hostile bidder’s shares at an above-market price. In addition to (or sometimes in lieu of) the premium paid for the shares, the target company often agrees to pay the expenses the bidder incurred in launching and then canceling the takeover. In return for the greenmail, the bidder usually agrees to refrain from purchasing the target’s stock for a specified period of time.

The Funds’ policy is to vote in favor of proposals to restrict a company from paying greenmail. Anti-greenmail proposals (whether they are management or shareholder proposals) typically call for a vote to amend the company’s charter and/or by-laws to prohibit the company from repurchasing any (or, in some cases, a certain percentage) of its outstanding common stock from any shareholder for a price in excess of the market value unless (i) the selling shareholder has held the shares for a specified number of years (generally, two years) and (ii) either the holders of a majority of the outstanding shares not owned by the potential acquiror approve the transaction or the same repurchase terms are offered to all shareholders.

Greenmail payments generally are not in the best interests of a company’s shareholders. The share price of a company that pays greenmail usually declines after the payment because the above-market premiums paid to the greenmailer are drawn from funds that could be reinvested in the company or paid in dividends to the shareholders, and greenmail payments are discriminatory to the other shareholders who are not given the opportunity to sell their shares at the per-share price paid to the greenmailer.

### 3.6 Opt Out of Delaware's Anti-Takeover Law: FOR

Section 203 of the Delaware General Corporation Law contains a “freeze out” provision which, in general, prohibits a company from entering into any business combination with an acquiror of 15% or more of the company’s stock for a period of three years after the acquisition by the acquiror of the shares. The freezeout does not apply if (i) the combination is approved by the company’s board of directors prior to the share acquisition, (ii) the combination is approved by the board and two-thirds of the shares held by persons other than the acquiror, or (iii) the acquiror ends up owning at least 85% of the outstanding shares. The statute provides that a company can elect not to be governed by the freeze out law if a majority of the outstanding shares votes to do so, and some shareholders have proposed amendments to their company’s charter or by-laws to opt out of the statute.

The Funds support proposals to opt out of Delaware’s takeover statute because a company that is subject to the law may deter potentially attractive takeover bids.

### 3.7 Supermajority Voting Requirements: AGAINST

A supermajority voting provision in a company’s charter or by-laws imposes, generally or as to one or more specified matters, a level of voting approval in excess of a simple majority of the outstanding shares. A supermajority vote requirement may be two-thirds, 80%, or in some cases, even higher. Management proposals to require a supermajority vote typically ask the shareholders to vote to approve an amendment to the company’s charter or by-laws requiring some higher than majority level of approval from the shareholders for a particular type of action, such as the removal of directors or mergers or other changes in control. Some argue that such requirements ensure broad shareholder agreement on issues that may have a significant impact on the company. The Funds generally oppose supermajority voting requirements. By requiring approval of greater than a majority of the voting shares in order to effect certain actions, a supermajority voting provision can be used as an antitakeover measure. The Funds generally support shareholder proposals calling for a company to eliminate one or more of the company’s existing supermajority voting provisions.

### 3.8 Preemptive Rights: AGAINST

A preemptive right gives shareholders of a company priority over non-shareholders in subscribing on a pro rata basis for any additional shares that the company may propose to issue in the future. Preemptive rights provisions generally give shareholders such rights as to any new shares that are to be issued for cash and which would dilute existing voting power or claims to dividends. Only if, and to the extent that, existing shareholders choose not to purchase newly issued shares, are outside investors permitted to purchase such shares. Under the laws in some states, shareholders are entitled to preemptive rights, unless the company’s charter provides otherwise. The laws of other states (including Delaware) provide that shareholders do not have preemptive rights unless such rights are expressly granted to the shareholders in the company’s charter. Management of companies whose charters provide for preemptive rights may initiate proposals to amend the charter to eliminate such rights. Shareholders, on the other hand, may submit proposals seeking to amend a company’s charter to include a preemptive rights provision or to restore preemptive rights provisions that were previously eliminated.

The Funds support proposals to eliminate preemptive rights and oppose proposals to restore preemptive rights. Preemptive rights result in the loss of financing flexibility for a company and can involve costly procedures. These added costs are not in the best interest of shareholders and are not justified because shareholders are able to purchase additional shares on the open market in order to maintain proportional ownership in the company.



### **3.9 Mergers, Sales, Acquisitions, And Other Business Combinations and Reorganizations, Recapitalizations, Spin-Offs, and Other Corporate Restructurings: CASE-BY-CASE ANALYSIS**

All Fund votes with respect to approval by shareholders of a merger, sale, acquisition, or other business combination (collectively, a “combination”) or a reorganization, recapitalization, or other corporate restructuring (collectively, a “restructuring”) are evaluated on a CASE-BY-CASE basis with full consultation of the Trust Committee. Fund votes will be based on a full analysis of any proposed combination or restructuring. Such analysis includes whether in connection with any proposed combination a fairness opinion was rendered and whether the terms of the proposed combination were negotiated at arm’s length. In the case of an acquisition or sale, the analysis includes the terms of any auction or bidding that was conducted in connection with the acquisition or sale. If in connection with a proposed combination or restructuring, the Funds, as shareholders of the company, would receive any consideration in exchange for a portion or all of the shares of stock they own in the company, the analysis should indicate whether the Funds will receive an amount equal to the current market value of the shares or some amount that deviates (either higher or lower) from the current market value. The Funds will also consider any other information that is relevant to a careful analysis of the proposed transaction and may consult with industry or equity analysts for their views on whether the Funds should vote in favor of or in opposition to the proposed transaction.

### **3.10 Fair Price Provisions: FOR**

Fair price provisions are designed to protect shareholders from two-tiered tender offers. Under the two-tier structure, shareholders will receive one price if they tender before the offeror obtains corporate control, and will be frozen out at a significantly lower price if they do not do so and the offeror obtains sufficient control to effect the plan. The practice is designed to coerce shareholders into tendering their shares early, even if they believe that the price is inadequate, by threatening them with an even lower price if others tender their shares. In essence, two-tier tender offers present shareholders with a “prisoner’s dilemma.” Fair price provisions generally require supermajority votes to approve mergers in which shareholders would receive less compensation per share than the highest prices the bidders have paid for any such shares within a certain period. These provisions are designed to combat the coercive effect of such bids.

Fair price provisions have been effective in preventing the coercive effect of two-tiered tender offers that penalize shareholders for declining unacceptable offers. The Funds believe that reducing this risk of severe loss enhances share values. Moreover, the Funds’ participants themselves will benefit from a fair price provision whenever, in the best judgment of the Funds, a tender offer is inadequate.

### **3.11 Confidential Voting: FOR**

The Funds support confidential voting systems in which only the proxy tabulator and inspector of elections know the identity of the shareholders and how they voted on each issue. The management of the company should be provided with information only on the total number of shares voted and the percent that voted for and against and abstained from voting on each proposal. A confidential voting system eliminates management’s ability to discover a shareholder’s vote without its consent. Proxy tabulators should be independent from management; company employees should not serve as vote tabulators. Accordingly, the Funds generally support shareholder proposals to establish confidential voting and to require independent voting tabulators.

### 3.12 Cumulative Voting: FOR

Cumulative voting entitles each shareholder to cast a number of votes equal to the number of shares owned multiplied by the number of directors to be elected. Under cumulative voting, a shareholder may cast all of its votes for one nominee or apportion them (equally or not) among two or more nominees. By casting all their votes for one nominee, a minority of shareholders can gain representation on the board of directors. The Funds generally support cumulative voting proposals because cumulative voting is an effective method of enabling small shareholders to promote director accountability, guaranteeing minority representation on a board of directors, and ensuring that the board is at least partly independent of management.

### 3.13 Shareholder Right to Act by Written Consent: FOR

The laws of most states permit a company's charter or by-laws to provide for shareholder action by written consent, without a meeting, on any matter on which the shareholders could act by formal vote at a formal meeting. Written consent allows shareholders to initiate and carry on a shareholder action without having to wait until the annual meeting and without having to call a special meeting. The level of shareholder approval required in order to take action by written consent depends on state law. Under the laws of most states, shareholder action by written consent requires unanimous shareholder approval. Action by written consent in some states (including Delaware), however, only requires the approval of the same percentage of the voting shares that would be required to effect the proposed action at a shareholder meeting.

Potential acquirors have occasionally attempted to gain control of a company by conducting proxy contests through the solicitation of written consent from the shareholders. In order to prevent this, management of a number of companies have proposed that the right of shareholders to take action by written consent be limited or eliminated.

The Funds support shareholders' right to act by written consent and oppose proposals to limit or eliminate shareholders' right to act by written consent. The Funds believe that action by written consent is a fundamental shareholder right. Shareholders should be able to take such measures at either shareholder meetings or at other points during the year through written consent. The Funds believe that formally established approval thresholds for any action taken by written consent protect shareholders from measures being enacted without the support of the majority of shareholders. Such benefits outweigh opponents' arguments that actions by written consent may prevent all shareholders from having complete and accurate information prior to taking action.

### 3.14 Shareholder Right to Call a Special Meeting: FOR

Under the laws of most states, a special meeting of the shareholders is required to be called by the company at the request of a specified percentage (generally 10% to 20%) of the voting shares. The corporate laws of some states (including New York and Delaware), however, provide that the percentage may be specified in a company's charter or by-laws.

Some companies have called for limitations on or the elimination of the ability of shareholders to call special meetings in order to prevent a potential acquiror who has acquired a sufficient percentage of shares from forcing management to call a meeting to address the takeover issue. Proposed limitations commonly include increasing the percentage of ownership required for a shareholder or group of shareholders to call a special meeting, limiting the frequency with which special meetings can be called by shareholders, and/or restricting the length of time any one shareholder could solicit other shareholders to agree to call a special meeting.



Shareholders, on the other hand, of companies whose charter and/or by-laws do not give shareholders a right to call a special meeting have submitted proposals calling for an amendment to the company's charter or by-laws to permit shareholders to call a special meeting upon the request of a certain percentage of the voting shares of the company. The Funds support shareholders' right to call a special meeting and oppose proposals to limit or eliminate shareholders' right to call a special meeting. The Funds believe that shareholders should have a fundamental right to convene a meeting of shareholders based upon a reasonable threshold of votes of outstanding shareholders. Limitations on such rights, in the Funds' view, may be used as antitakeover measures. Moreover, by prohibiting shareholders from calling a special meeting, all action is forced to take place at an annual meeting, which can cause long delays in resolving important issues.

### 3.15 Reincorporation: CASE-BY-CASE ANALYSIS

A reincorporation proposal, submitted by either management or shareholders, has considerable implications for shareholders because reincorporation may affect the company's takeover defenses and its corporate governance features. Because a company that reincorporates will be subject to the laws and courts of a different state or country, the differences between the laws of the old and new jurisdictions also could have an effect on the company. In addition, companies frequently make other significant changes in their charters and by-laws when they reincorporate and therefore these provisions should be reviewed carefully.

The Funds may support proposals to reincorporate from one jurisdiction to another if satisfactory business reasons are cited and there are no significant negative impacts on corporate governance or management accountability.

The Funds generally oppose proposals by companies to reincorporate to jurisdictions that would result in a weakening of shareholder rights or present other risks (such as weaker management accountability or adverse impact on company employees or their communities) that outweigh potential benefits. This pertains to reincorporations from one state to another as well as to other countries.

The Funds generally support shareholder proposals to block or prohibit companies from reincorporating in other countries and support proposals urging companies to reincorporate in the United States in order to increase management accountability, improve governance or enhance the rights of shareholders.

The Funds may oppose a proposal to reincorporate a company in a different state or country for one or more of the following reasons:

**(i) Antitakeover Defenses.** If the laws of the proposed state or country of incorporation permit a company to adopt stronger antitakeover defenses (such as "poison pills") than the laws of the current state or country of incorporation, the Funds may oppose the proposal to reincorporate. The Funds also may oppose a reincorporation proposal if the laws of the proposed state or country of incorporation include a greater number of and/or stronger anti-takeover provisions (such as control over share acquisition and freeze-out statutes) than the current state or country of incorporation.

**(ii) Director and Officer Liability.** If the laws of the proposed state or country of incorporation permit a company to provide for greater limitations on directors' and officers' liability than the laws of the current state or country of incorporation, the Funds may oppose the proposal to reincorporate.

**(iii) Shareholder Democracy.** If the laws of the proposed state or country of incorporation impose more limitations on shareholders' rights (such as limitations on the right to act by written consent or to call a special meeting) than the laws of the current state or country of incorporation, the Funds may oppose the proposal to reincorporate.

(iv) **Corporate Governance.** If the laws of the proposed state or country of incorporation permit a company to classify its board and the laws of the current state or country of incorporation do not, the Funds may oppose the proposal to reincorporate.

(v) **Amendment of Company's Charter or By-laws.** If, in conjunction with reincorporation, the company proposes to amend its charter or by-laws in such a manner that the Funds would oppose the amendment if it were presented as a separate proposal (for example, an amendment to impose supermajority voting requirements or to eliminate cumulative voting), the Funds generally will oppose the proposal to reincorporate.

### **3.16 Judicial Forum or Venue: AGAINST**

The Funds generally oppose efforts to restrict or otherwise limit shareowners' right to select the appropriate judicial venue by adopting exclusive venue governance provisions.

## **4. Executive Compensation**

### **4.1 Advisory Votes on Executive Compensation**

The Funds support executive compensation policies and practices that are aligned with shareholders' interests and drive sustainable value creation on behalf of shareholders. Since compensation design and practices play a key role in defining incentives for senior executives, the Funds support efforts to provide shareholders with an advisory vote on executive compensation.

#### **4.1a Shareholder Proposals Calling for Advisory Votes on Executive Compensation: FOR**

The Funds believe companies should provide shareholders an advisory vote to enable investors to express their opinion about the general compensation philosophy of the board and how compensation awards to executives align with the principles of "pay for performance." In the Funds' view, providing for a non-binding, advisory vote on the board of director's compensation committee report will allow shareholders to register their views on whether the compensation practices of a company are aligned with the long-term interests of shareholders.

#### **4.1b Advisory Votes on Executive Compensation: CASE-BY-CASE ANALYSIS**

The Funds vote on a CASE-BY-CASE basis whether to support management proposals requesting that shareholders, through a non-binding vote, ratify the compensation report of named executive officers in the company's proxy statement. Among the factors that should be weighed in considering support for the executive compensation report are:

- Extent to which "pay for performance" principles govern the compensation policies and practices of senior executives, including the relation of the company's executive compensation to its peers and industry medians, the relation of the company's long-term financial performance to relevant peers in its sector, and the presence of clearly-defined, broad-based metrics in establishing criteria for incentive compensation;
- Existence of egregious pay practices, such as excessive golden parachutes or other severance provisions, excessive dilution rates in equity plans, extensive "gross-up" provisions limited to senior executives, or other provisions which are not justified in a "pay-for-performance" philosophy;
- Clarity of disclosure and reporting of all significant components of executive compensation;
- Extent to which, viewed in its entirety, the compensation practices of the company align executives' interests with the long-term interest of shareholders.

#### 4.1c Frequency of Advisory Votes on Executive Compensation: ANNUAL

The Funds believe that, in order to be an effective tool for communication between a company and its shareholders, advisory votes on executive compensation should be held on a regular and routine basis. In the United States, companies must query investors, on an advisory basis, at defined intervals whether to hold advisory votes on an annual, biannual, or triennial basis. Companies make decisions on compensation practices, including bonuses and incentive compensation, on an annual basis. Therefore, it is the view of the Funds that companies should implement advisory votes on executive compensation on an annual basis. Annual advisory votes promote regular communication with shareholders and avoid unnecessary delays in gauging any shareholder concerns about pay practices.

#### 4.2 Equity and Incentive Compensation Plans: CASE-BY-CASE ANALYSIS

The Funds vote on equity and incentive plans based upon CASE-BY-CASE analysis of the proposed plan and its features. The Funds generally support fair, adequate, and reasonable equity and incentive plans and amendments to such plans. The Funds believe that the granting of equity and incentives to senior executives plays a key role in defining objectives for shareholder value growth and thereby can help align the interests of executives with the shareholders of the company.

Management proposals call for shareholders to approve adoption of an equity or incentive plan or to approve an amendment or amendments to a plan. (Typical proposals to amend existing plans call for an increase in the number of shares issuable under the plan or extension of the term of the plan.) Shareholder approval is required to adopt or make material amendments to most equity and incentive plans. Appendix B sets forth a discussion of various types of awards granted under equity and incentive compensation plans and certain features of such plans.

The Funds vote against proposed plans that fail to demonstrate an alignment between shareholders interests and the incentives for executives described in the proposal, provide executives with excessive benefits, or contain provisions that place shareholder value at risk.

In determining how to vote, the Funds consider the following guidelines:

- **Specific Performance Standards.** The purpose of equity and incentive plans should be to reward a company's employees for superior past performance in carrying out their responsibilities and to encourage the same efforts in the future. Consequently, the proposed plans should specify how the granting of equity will be tied to an employee's and the company's performance. If the proposed plan does not provide sufficient information for the Funds to determine the plan's employee or company performance standards and the factors in determining the amount of options or incentives to be granted by the company to the employee, the Funds generally vote against the proposed plan.
- **Dilution.** The Funds generally vote against adoption of plans or plan amendments if the equity granted or other rights issuable under the plan could dilute the earnings per share of the outstanding shares of the company by more than 5% (calculated by dividing the number of shares reserved for issuance under the plan by the number of the company's outstanding shares). The Funds also may consider the aggregate dilutive effect of all equity plans adopted by a company, to the extent information regarding such other plans is available.
- **Discount Options and Underwater Awards.** The Funds generally vote AGAINST adoption of plans or plan amendments that contain these features.

- **Other Features of Plans.** If a proposed plan includes specific performance standards for the grant of equity that serve as a reasonable reward for past superior performance and as an incentive for future superior performance, and if it results in 5% or less dilution, the Funds will evaluate the other features of the plan to determine whether to vote in favor of or in opposition to the plan. The Funds' policy may vote against adoption of a plan or plan amendment if the plan includes two or more of the following features:
- **Reload Options.** The plan includes reload options which allow the company to replace stock already given in the exercise of an option.
- **Replacing or repricing underwater awards or grants.** The plan allows the company to swap options at a lower stock price or to lower the exercise price of options already granted. (An exception may be considered if the decline in stock price results from a market wide phenomenon rather than company specific performance and senior executives are excluded from repricing outstanding awards or grants.)
- **Pyramiding.** The plan permits pyramiding, which enables plan participants to pay for stock options with previously owned shares in successive short term transactions, thus pyramiding a small amount of stock into a larger holding.
- **Discount Options.** The plan provides for options with an exercise price that is substantially below (less than 85%) the market value of the stock on the date of grant.
- **Change in Control Features.** The plan provides for acceleration of the vesting of options upon a change in control of the company or contains other change in control features unfavorable to shareholders.
- **Time-lapsing Restricted Stock.** Restricted stock which is not tied to corporate or individual performance may be issued pursuant to the plan.
- **Omnibus Plan.** The plan gives the compensation committee or the board of directors broad discretion to decide how much and what type of stock to award and when and to whom to make such awards.
- **Evergreen Plan.** The plan is an "Evergreen Plan" because it has no termination date and thus may result in excessive dilution over an extended period of time

#### 4.3 Pay-for-Performance: CASE-BY-CASE ANALYSIS

The Funds believe that executive compensation policies and programs should be rooted in a "pay-for-performance" philosophy. The Funds review shareholder proposals seeking to ensure that executive pay levels are linked to corporate performance on a CASE-BY-CASE basis.

The Funds generally support shareholder proposals to tie executive compensation to company performance unless (i) the company's performance (measured by total shareholder return) over the previous five years is above the average performance of the companies in its industry peer group, and (ii) the company's compensation committee (or the full board of directors if no compensation or comparable committee has been appointed) is composed of a majority or entirely of independent directors. The Funds believe that by linking executive pay to company performance, the interests of executives will be more closely aligned with those of shareholders.

The Funds believe that if a company is performing well and its compensation committee (or the full board of directors if no compensation or comparable committee has been appointed) is composed of a majority of independent directors, the company's compensation committee (or the full board of directors if no compensation or comparable committee has been appointed) is in the best position to determine the appropriate compensation policies of the company's executives.

#### **4.4 Disclosure of Integrating Executive Compensation with Sustainability Risks: FOR**

The Funds believe that executive compensation practices should drive sustainable shareholder growth. As such, the Funds believe that compensation policies should be attentive to risks to long-term, sustainable returns. An asymmetry may occur when compensation incentives deliver awards based on annual, three-year, or five-year incentive programs, for example, but long-term risks to value creation may emerge in later years. Accordingly, the Funds support company efforts to integrate sustainability metrics, such as worker health and safety, environmental performance, diversity in workplace practices, and other appropriate metrics, which may serve to promote long-term shareholder value and avoid legal, regulatory, operational, or reputational risks for the company. The Funds generally support reasonable proposals requesting that a company report on how it links executive compensation to the company's financial, social, and environmental performance.

#### **4.5 Severance Agreements and Golden Parachutes**

A "golden parachute" is a severance agreement between a company and a senior executive that takes effect upon a change in control of the company. Golden parachutes usually provide the executive with cash payments equal to a multiple (two to three times) of the executive's annual compensation and certain non-cash benefits if he or she is terminated, demoted, or resigns within a specified period of time after the change in control of the company. Severance agreements similar to golden parachutes but which cover a broader range of employees, often are referred to as "silver" or "tin" parachutes.

##### **4.5a Proposals to Obtain Shareholder Approval for Parachutes: FOR**

The Funds support proposals to require a company to obtain approval of future golden, silver, or tin parachute agreements. The Funds believe that the shareholders should decide whether or not it is in their best interests for the company to enter into such agreements and whether the terms of such agreements do not unnecessarily drain corporate resources.

##### **4.5b Proposals to Approve Severance Payments in Connection with a Merger or Acquisition: CASE-BY-CASE ANALYSIS**

The Funds analyze whether to approve severance provisions of mergers and acquisitions on a CASE-BY-CASE basis, assessing whether such provisions are rooted in performance, are in line with peer practices, do not constitute an unreasonable expense to the corporation, and do not contain egregious provisions such as grossups or accelerated vesting of equity.

##### **4.5c Proposals to Prohibit Commitments to Pay Excise Tax "Gross-Ups:" FOR**

The tax code prohibits companies from taking deductions for excess parachute payments and imposes a nondeductible 20% excise tax (which the employer is required to withhold) upon the receipt of any such payment. The code defines a parachute payment as any compensatory payment made to an executive or director that is contingent upon a change in control. A parachute payment is considered "excessive" and subject to the tax provisions described above if the payment exceeds 300% of the executive's average annual taxable compensation for the five most recently completed taxable years. Any payment made within one year of a change in control is considered a parachute payment. Many companies have included "gross-up" payments as part of their parachute agreements to offset any excise tax the executive would be required to pay.

The Funds oppose “gross-up” payments and believe that executives should be responsible for paying their own income taxes. The Funds support proposals to prohibit any future commitments by companies to pay tax “gross-ups” on severance arrangements.

#### **4.5d Proposals to Prohibit Accelerated Vesting of Unearned Equity: FOR**

Equity plans generally are designed to reward executives for specific performance goals. Some equity plans contain provisions to disregard performance goals and other vesting provisions for equity awards upon changes-in- control. The Funds oppose accelerated vesting of equity awards and believe that equity awards should only be granted upon actual attainment of specified goals. Accelerated vesting can be costly to shareholders. The Funds support proposals to prohibit accelerated vesting of unearned equity.

#### **4.6 Clawbacks and Recoupment Policies: FOR**

The Funds believe that incentive compensation can be a useful way to reward and motivate senior executives, and the Funds support “pay for performance” programs that suitably reward executives for “hitting their numbers.” The Funds also believe, however, that if executives are rewarded when they did not hit their numbers, they should not retain money they did not earn. In those situations the board of directors should review compensation paid during restatement periods and, to the extent practicable, seek to recoup money that was paid when the targeted results were not met. Companies should have defined “clawback,” or incentive recoupment policies that if the company restates its financial results, the board will review all bonuses and other awards made to senior executives during the period subject to the restatement and will, to the extent practicable, recover or cancel any such awards that were based on targets that would not have been met under the restated financial results.

#### **4.7 Restrictions on Executive Compensation: AGAINST**

Shareholder proposals to limit executive compensation come in a variety of forms. Some proposals call for a cap on executive pay at a specified level or a multiple of the average company employee’s salary. Others restrict certain forms of compensation. The Funds will generally oppose proposals that impose an arbitrary and overly restrictive cap on compensation levels or pay provisions. The Funds believe that the compensation committee, if comprised of entirely independent directors, should be empowered to design appropriate pay levels without being subject to arbitrary limitations. Moreover, arbitrary limits on executive compensation may have unintended consequences that could be detrimental to shareholder value. Where the Funds perceive pay to be decoupled from performance, the Funds will register their disapproval via the company’s advisory vote on executive compensation and other proxy measures, as appropriate.

#### **4.8 Non-Executive Director Compensation**

##### **4.8a Proposals to Grant Equity or Awards to Non-Employee Directors: CASE-BY-CASE ANALYSIS**

Non-executive directors may receive compensation for their service to the Board, including an annual retainer, and payments for meeting attendance, committee membership, and other functions, in a variety of forms, including cash and equity. Companies that award directors with equity may provide outright payments of equity on an annual basis or one-time awards or may provide for non-executive director participation in equity plans. The Funds evaluate on a CASE-BY-CASE basis management proposals asking shareholders to vote to either approve amendments to existing equity plans to include executive directors as eligible participants or to vote to approve the adoption of a separate equity plan covering non-employee directors. The Funds will consider supporting reasonable equity plans for outside directors if they are tied to specific and reasonable performance and attendance standards, are in lieu of cash compensation, or are designed to make the directors’ total compensation package competitive.



Outside directors who are granted equity in lieu of a portion of the annual retainer may accumulate a financial stake in the company, which in turn creates an incentive to maximize the value of the company's shareholder value. The Funds oppose the granting of equity to outside directors if the directors are paid a competitive cash compensation and the equity is not tied to specific and reasonable performance and attendance standards. Such equity potentially causes conflicts of interest, and may make directors less willing to challenge management or to take a long-term approach to decisions.

#### **4.8b Prohibit Extending Retirement Benefits to Non-Executive Directors: FOR**

The independence of non-employee or outside directors may be compromised by the prospect of retirement benefits that encourage outsiders' alignment with management (board members who also manage a company establish the benefits for outsiders). The Funds support such proposals based on their belief that the adoption of retirement benefits for non-employee or outside directors may diminish such directors' ability to act objectively and independently of management.

#### **4.9 Equity Ownership for Executives and Directors: FOR**

The Funds believe that equity ownership aligns executives' and directors' interests with those of shareholders. Accordingly, the Funds support reasonable proposals that request that companies adopt policies to require executives and directors to acquire a specified minimum number of shares or minimum value of shares of the company's equity. In order to avoid deterring otherwise qualified directors from being able to serve on the board, director equity ownership requirements should afford directors a reasonable amount of time to accumulate the requisite number or value of shares. The Funds also support proposals to require that some reasonable amount of directors' compensation be made in equity.

#### **4.10 Prohibit Insider Trading: FOR**

The Funds support policies and proposals to prohibit insider trading in their stock. Insider trading can undermine the public's confidence in companies, thereby depressing share prices. Under section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5, "insider trading" consists of a transaction in stock of a publicly held corporation by an insider who bases his or her trading on advance or inside information. The term "insider," in general, describes a person who has a relationship with the corporation in question affording access to information that should only be available for a corporate purpose. The practice is a federal felony, punishable by fine, imprisonment, or both. Although insider trading is already subject to criminal punishment, the Funds believe it is advantageous for companies to further deter the practice by stating clear policies against it and taking appropriate action when those policies are violated.

#### **4.11 Responsible Use of Company Stock: FOR**

The Funds believe that directors and senior executives who are in a position of exercising oversight for business strategies or implementing business strategies for value creation on behalf of shareholders should have a long-term interest in their own holdings in company equity. Such long-term interest best aligns directors' and executives' interests with long-term shareholders, such as the Funds. Accordingly, the Funds support policies and proposals that ask companies to adopt policies that prohibit insiders, such as board directors and senior executives, from hedging the value of their company equity or pledging company shares as collateral to margin accounts. Margin calls can occur when a company's share price is already under pressure. If there is a margin call, a significant number of shares held by a senior executive or director may be suddenly dumped on the market, which can further depress the share price.

Such a result can be detrimental to shareholders as a whole. Similarly, if holdings in company stock are subject to hedging activity, senior executives and directors may be better protected against price drops than shareholders generally. Margin trading and hedging in company equity both create potential conflicts of interests between an insider's holdings and long-term shareholders' interests. The Funds support proposals to promote responsible use of company stock by directors and senior executives, which policy would bar derivative or speculative transactions involving company stock, including but not limited to trading in puts, calls, covered calls or other derivative products; engaging in hedging or monetization transactions with respect to company stock; holding company stock in a margin account; or pledging company stock as collateral for a loan.

#### **4.12 Employee Share Ownership Plans: CASE-BY-CASE ANALYSIS**

The Funds generally support the adoption of employee stock purchase plans ("ESOP"). These plans, which usually allow employees to purchase shares of company's stock at the market price or at a slight discount from the market price, encourage employee ownership in the company. They typically cover a large number of employees of the company, including lower level employees. The Funds believe employee stock ownership helps to align the interests of the employees of the company with the interests of the shareholders in increasing the value of the company's equity. As a result, these plans may improve company productivity and efficiency. However, if the ESOP is constructed in a way that disadvantages employees, the Funds would vote against the plan. In determining how to vote, the Funds will consider factors such as whether hourly employees receive equity on a fair monetary basis vis-a-vis other employees; whether adequate voting rights adhere to employee-owned shares; and whether employees suffer adverse impact on pension or other benefits.

## **5. Environmental and Social Issues**

### **5.1 Environmental Issues and the CERES Principles**

The CERES Principles are a ten-point code of conduct that promotes environmental responsibility and sustainability in corporate activities. These principles create a standard for measuring a company's treatment of the environment and are intended to assist investors in making informed decisions regarding business risks and opportunities that companies may face regarding environmental issues.

The CERES Principles were developed in 1989 by the Coalition for Environmentally Responsible Economies (CERES), which is comprised of investors, environmental organizations, and public interest groups. Appendix C contains the complete guidelines.

#### **5.1a Proposals Requesting Commitment to Support CERES Principles: FOR**

The Funds encourage portfolio companies to adopt the CERES principles, or their own comparable codes, in order to commit to measuring and disclosing business risks and opportunities related to the environmental impact of the companies' operations. Moreover, the CERES principles help guide portfolio companies to address issues that may impact long-term shareholder value.

#### **5.1b Proposals Requesting Public Reporting on Environmental Practices: FOR**

The Funds believe that investors benefit from standardized and transparent reporting from companies on issues related to the CERES principles. Individual firms' attention to environmentally sustainable practices, such as reducing pollution, can have a positive impact for the overall market, promote a viable and sustainable economy, and are therefore in the long-term interests of shareholders. Disclosure of a company's environmental policies and practices can encourage environmentally responsible practices and compliance with all applicable environmental laws. Accordingly, the Funds will generally support reasonable proposals calling for public reporting of environmental issues.



### **5.2 Political Contributions Disclosure: FOR**

The Funds believe that corporate expenditures on lobbying as well as corporate contributions in support of or in opposition of political candidates and/or campaigns create certain legal, compliance, and reputational risks. Accordingly, the Funds support reasonable proposals that call on Boards of Directors to exercise oversight and transparency by reviewing and publicly reporting on a regular basis all such expenditures or contributions from corporate assets. Greater transparency helps mitigate inherent risks in political involvement, enables shareholders to determine if a company's contributions or expenditures in this area are being directed in a manner that is consistent with the long-term interests of the company and its shareholders, and also helps to safeguard corporate assets from being deployed under the influence of individual political preferences of corporate officers.

### **5.3 Charitable Contributions: CASE-BY-CASE ANALYSIS**

Business philanthropy has become a significant and well-established practice. The Funds generally support Board oversight and transparency of significant uses of corporate assets, including charitable giving. However, the Funds generally oppose overly prescriptive proposals that direct a corporation to donate or cease donating to specific organizations. In assessing proposals, the Funds evaluate the propensity for the request to provide shareholders with valuable information and to improve or safeguard long-term shareholder value.

### **5.4 Equal Employment Opportunity: FOR**

The Funds support the development of robust policies to promote equal employment opportunities for all employees and support reasonable requests for companies to disclose and report on the implementation of such policies. Discrimination in employment on the basis of age, sex (including pregnancy), race or ethnicity, national origin, genetic information, religion, sexual orientation, disability, veteran status, or other factors unrelated to work performance create legal and operational risks for companies and may undermine productivity and shareholder value.

### **5.5 High-Performance Workplaces: FOR**

The Funds believe that long-term productivity enhancement strategies improve share value and lend stability to companies. High-performance workplace proposals seek to promote productivity through various measures. The Funds generally support reasonable proposals to promote enhanced productivity through human resource investments, training and skills development, and labor-management cooperation.

### **5.6 Human Rights and Codes of Conduct: FOR**

The Funds believe that portfolio companies should abide by international human rights conventions throughout their operations and take proactive steps to define their standards or expectations for human rights, develop appropriate systems to monitor their internal compliance with such standards, and where appropriate, publicly report on such compliance. Through a company's operations, both globally and domestically, companies face legal, regulatory, operational, and reputational risks when they or their suppliers violate international human rights conventions. When guilty of human rights violations, or even when associated with human rights violations (such as political regimes with track records of non-compliance), companies may place shareholder value at risk and may damage their continued operations. Accordingly, the Funds support reasonable proposals to establish, monitor, and/or report on human rights standards and compliance.

### **5.7 Corporate Activity in Northern Ireland – The MacBride Principles: FOR**

The MacBride Principles (see Appendix D), which were first proposed in 1984 by Nobel Peace Prize winner Sean MacBride, are a set of nine equal opportunity/affirmative action principles aimed at fighting religious discrimination in employment in Northern Ireland.

The Funds support proposals that request a company to implement and report on the implementation of the MacBride Principles. The Funds believe that the MacBride Principles are a means by which companies can promote equal employment opportunity, mitigate the legal and reputational risks of employment discrimination, and promote a meaningful peace which is conducive to a stable economy and investment environment.

#### **5.8 Health Care Policy: FOR**

The Funds believe that broad access to affordable, cost-effective, and efficacious health care may enhance individual firm profitability and performance, and promote corporate growth and financial stability at individual firms and across the marketplace. High healthcare costs and incomplete or inadequate insurance coverage, on the other hand, may have detrimental impacts on profitability and performance. Accordingly, the Funds support reasonable proposals for companies to review and publicly report on the impact of health care policy reforms.

#### **5.9 Access to Medicine: FOR**

Broad access to affordable and effective medicines may broaden the consumer market for individual firms and promote stable conditions for economic growth in lower-income markets. The Funds recognize that HIV/AIDS, tuberculosis, malaria, and other pandemics constitute public health crises in numerous global markets and threaten stable economic growth. The Funds support reasonable proposals requesting companies to report to shareholders on the impact of diseases and global health crises on the companies' strategies for shareholder growth and the impact of pricing strategies on promoting access to medicines. The Funds believe that clear disclosure of the legal, regulatory, marketing, and reputational risks of access to medicines are in the long-term interests of shareholders.

#### **5.10 Tobacco Advertising and Production: CASE-BY-CASE ANALYSIS**

Tobacco advertising creates certain legal and reputational risks for companies which may ultimately have a negative economic impact on the company. To mitigate such risks, the Funds generally support proposals requesting that companies adhere to reasonable standards for advertising, report to shareholders regarding their advertising of tobacco products, or assess the impact of their tobacco advertising on consumer markets. The Funds generally oppose proposals for companies to stop selling tobacco and tobacco-related products, as the Funds believe that it is not in shareholders' economic interests to discontinue sales of a legal product.

#### **5.11 Animal Protection: CASE-BY-CASE ANALYSIS**

Animals can be an integral part of product safety testing. Most experiments relate to biomedical research and the testing of pharmaceuticals and chemicals. Only a small fraction of animal use is for the testing of non-medical consumer products, such as cosmetics and household products.

The Funds generally support proposals to prohibit animal testing that is not required by law, unless management advances compelling business reasons against an absolute prohibition. The Funds believe that animal testing, in some cases, may be unnecessary and cruel to animals.

The Funds generally oppose proposals to phase out products that are tested on animals, as the Funds believe that animal testing may be necessary for the company to protect itself against lawsuits or to ensure the safety of the product, and accordingly, any phase out may be detrimental to shareholder value.

The Funds generally abstain on requests for companies to report on the use of live animals in testing.

## Appendix A

### Council of Institutional Investors

#### Definition of Director Independence

A director will not be considered independent if he or she:

a. Is, or in the past five years has been, or whose relative is, or in the past five years has been, employed by the corporation or employed by or a director of an affiliate;

**Notes:** An “affiliate” relationship is established if one entity either alone or pursuant to an arrangement with one or more other persons, owns or has the power to vote more than 20 percent of the equity interest in another, unless some other person, either alone or pursuant to an arrangement with one or more other persons, owns or has the power to vote a greater percentage of the equity interest. For these purposes, joint venture partners and general partners meet the definition of an affiliate, and officers and employees of joint venture enterprises and general partners are considered affiliated. A subsidiary is an affiliate if it is at least 20 percent owned by the corporation. Affiliates include predecessor companies. A “predecessor” is an entity that within the last five years was party to a “merger of equals” with the corporation or represented more than 50 percent of the corporation’s sales or assets when such predecessor became part of the corporation. “Relatives” include spouses, parents, children, step-children, siblings, mothers and fathers-in-law, sons and daughters-in-law, brothers and sisters-in-law, aunts, uncles, nieces, nephews and first cousins, and anyone sharing the director’s home.

b. Is, or in the past five years has been, or whose relative is, or in the past five years has been, an employee, director or greater-than-20-percent owner of a firm that is one of the corporation’s or its affiliate’s paid advisers or consultants or that receives revenue of at least \$50,000 for being a paid adviser or consultant to an executive officer of the corporation;

**Notes:** Advisers or consultants include, but are not limited to, law firms, auditors, accountants, insurance companies and commercial/investment banks. For purposes of this definition, an individual serving “of counsel” to a firm will be considered an employee of that firm. The term “executive officer” includes the chief executive, operating, financial, legal and accounting officers of a company. This includes the president, treasurer, secretary, controller and any vice-president who is in charge of a principal business unit, division or function (such as sales, administration or finance) or performs a major policymaking function for the corporation.

c. Is, or in the past five years has been, or whose relative is, or in the past five years has been, employed by or has had a five percent or greater ownership interest in a third-party that provides payments to or receives payments from the corporation and either: (i) such payments account for one percent of the third-party’s or one percent of the corporation’s consolidated gross revenues in any single fiscal year; or (ii) if the third-party is a debtor or creditor of the corporation and the amount owed exceeds one percent of the corporation’s or third party’s assets. Ownership means beneficial or record ownership, not custodial ownership;

d. Has, or in the past five years has had, or whose relative has paid or received more than \$50,000 in the past five years under, a personal contract with the corporation, an executive officer or any affiliate of the corporation;

**Notes:** Council members believe that even small personal contracts, no matter how formulated, can threaten a director's complete independence. This includes any arrangement under which the director borrows or lends money to the corporation at rates better (for the director) than those available to normal customers—even if no other services from the director are specified in connection with this relationship;

e. Is, or in the past five years has been, or whose relative is, or in the past five years has been, an employee or director of a foundation, university or other non-profit organization that receives significant grants or endowments from the corporation, one of its affiliates or its executive officers or has been a direct beneficiary of any donations to such an organization;

**Notes:** A "significant grant or endowment" is the lesser of \$100,000 or one percent of total annual donations received by the organization.

f. Is, or in the past five years has been, or whose relative is, or in the past five years has been, part of an interlocking directorate in which the CEO or other employee of the corporation serves on the board of a third-party entity (for-profit or not-for-profit) employing the director or such relative;

g. Has a relative who is, or in the past five years has been, an employee, a director or a five percent or greater owner of a third-party entity that is a significant competitor of the corporation; or

h. Is a party to a voting trust, agreement or proxy giving his/her decision making power as a director to management except to the extent there is a fully disclosed and narrow voting arrangement such as those which are customary between venture capitalists and management regarding the venture capitalists' board seats. The foregoing describes relationships between directors and the corporation. The Council also believes that it is important to discuss relationships between directors on the same board which may threaten either director's independence. A director's objectivity as to the best interests of the shareowners is of utmost importance and connections between directors outside the corporation may threaten such objectivity and promote inappropriate voting blocks. As a result, directors must evaluate all of their relationships with each other to determine whether the director is deemed independent. The board of directors shall investigate and evaluate such relationships using the care, skill, prudence and diligence that a prudent person acting in a like capacity would use.

Council of Institutional Investors Corporate Governance Policies last updated Sept. 29, 2010.

## Appendix B

### Equity and Incentive Compensation Plan Definitions

#### Types of Awards:

The types of awards granted under stock option plans can vary widely. The most frequent awards include grants of stock options (both nonqualified stock options and incentive stock options, which are discussed below), stock appreciation rights (SARs), restricted stock and/or performance shares. Other less common types of awards include phantom shares and reload options. These awards are discussed in more detail below.

**(i) Stock Options.** Stock options give executives the right to purchase shares of their own company's stock at a specified price within a specified time period. After a certain period of time, the options vest and become exercisable, which means the option holder can pay the per share exercise price to purchase all or a portion of the shares covered by the option. If the market price of the stock is higher than the price at which the executive could exercise his or her option to purchase the stock, the options are considered "in-the-money" and the executive is guaranteed a profit if he or she exercises the options and then sells the stock received.

Stock options are either incentive (or qualified) stock options (ISOs) or nonqualified stock options (NSOs).<sup>\*</sup> The principal difference between ISOs and NSOs is the tax treatment of any gain at the time of exercise of the option. The holder of an ISO does not incur a tax liability upon exercise, but instead is taxed when the stock itself is sold, normally at capital gain rates. When the option being exercised is a NSO, however, the executive incurs a tax liability on any gain at the time of exercise and the gain is taxed as ordinary income. In 1986, however, the tax code was revised to equalize the tax rates for capital gains and ordinary income. As a result, NSOs became much more attractive to executives primarily because NSOs may be priced at less than fair market value, while the exercise price of ISOs must be equal to the market price on the date of the grant. In addition, NSOs have always been more attractive to companies because they may take a tax deduction when their employees exercise NSOs, but no tax deductions are allowed for ISOs.

In 1990, the tax code was again changed to increase the stated maximum marginal income tax rate from 28% to 31% and to place a maximum top tax rate of 28% on net capital gains. Therefore, an executive who is in the highest income tax bracket and is issued an ISO enjoys a lower tax rate (a 28% capital gain rate compared to a 31% marginal income tax rate if the option issued were a NSO) and the ability to defer his tax obligation until the stock underlying the option is sold (rather than upon exercise of the option if the option were a NSO).

**(ii) Stock Appreciation Rights (SARs).** Like ISOs and NSOs, SARs are granted with a per share exercise price and cover a specified number of shares. Upon exercise, however, instead of purchasing the shares at the exercise price, the holder of the SARs receives the "spread" between the market price and the exercise price, which may be paid in cash or shares of stock. If the SARs are granted in tandem with options, the holder may exercise either the option or the SAR.

<sup>\*</sup> For an incentive option to qualify for such tax treatment, it must satisfy a number of conditions stipulated in Section 422A of the Internal Revenue Code, including:

(i) the stock option plan must indicate the total number of shares that may be issued and identify the employees or class of employees that qualify; (ii) the plan must be approved by shareholders within twelve (12) months before or after its adoption by the board of directors; (iii) options must be granted within ten (10) years of adoption or shareholder approval, whichever is first, and granted options must be exercised within ten (10) years of the grant; (iv) the exercise price of the option may not be less than the market price of the stock at the time the option is granted; and (v) no individual may exercise incentive options worth more than \$100,000 in a single year.

**(iii) Restricted Stock.** Restricted stock awards are conditional grants of the company's common stock. They usually have a minimum holding period (generally, five years) before the executive can sell the stock. In the meantime, executives with restricted stock generally can vote the stock and are entitled to dividends with respect to such stock. The use of restricted stock has increased, in part, because it has no (or a minimal) exercise price. An executive is compensated therefore even if the market price of the stock does not rise. Variations on restricted stock awards include restricted shares or units that vest based on the attainment of specific performance objectives and restricted cash awards which have fixed-dollar amounts and are earned through continued employment.

**(iv) Performance Shares.** Performance shares are stock awards with vesting requirements based on the attainment by the company or the individual of certain performance goals. Some stock options or long-term performance incentive plans award executives with company shares or units that are contingent upon meeting certain performance objectives over a period of generally three to five years. The value of the performance shares or units depends on whether and the extent to which the performance goals have been met by the end of the performance period. Performance measures often are tied to growth in the company's stock price or earnings per share. They also may be tied to a comparison with the company's industry group or some other market indicator. Payments are made in cash, stock, or both and a tax liability is incurred on the date the awards are actually granted.

**(v) Phantom Stock.** Phantom stock is another type of market-based incentive compensation. Under some incentive plans, employees are awarded phantom stock (or bonus units) that correspond in number and value to a specified number of common shares. The phantom stock itself has no ownership interest, but is valued the same as the common shares. When the phantom stock matures, the payoff is based on the current value of the company stock and paid in cash or stock. The executives incur no tax liability when shares of phantom stock are awarded — only when benefits are paid. The benefits are taxed as ordinary income and issuing companies may deduct the income realized by employees as a business expense. If a phantom stock unit is paid in actual stock, any subsequent gains from holding the stock are taxed as capital gains.

**(vi) Reload Options.** Reload options are granted when an executive exercises options by exchanging shares that he or she already owns. The new reload option is for a number of shares equal to the number exchanged in the exercise and is issued at the market price on the reload date. The new option may be held for the remainder of the original option's term. The example below explains how a reload option works in practice.

**Example:** Mr. Smith currently owns 800 shares of company stock, which has a market price of \$50 per share. He also holds options to purchase 1,000 shares at an exercise price of \$40 per share. Four years of the options' ten-year term have lapsed. Smith exercises his options to purchase the 1,000 shares by exchanging the 800 shares he owns (which have a market value equal to \$40,000, calculated by multiplying 800 shares times the \$50 per share market price) to cover the purchase of the 1,000 shares issuable upon exercise of the options. He now owns 1,000 shares with a market value of \$50,000 (which is equal to 1,000 shares times \$50 per share) and receives a reload option for 800 shares with an exercise price of \$50 and a term of six years. At the end of the ten-year period, the stock price has risen to \$100 per share and Smith now exercises his reload option. The reload option is worth \$80,000 (which is equal to 800 shares at \$100 per share) but priced at \$40,000 (800 shares at the \$50 per share exercise price), and he can exercise the option with 400 of the shares he already owns (400 shares at \$100 per share). Smith would then own 1,400 shares (800 from the recent exercise and 600 left over from the shares he received in year four) which are worth \$140,000. The profit on the two transactions is \$100,000 (\$140,000 less the \$40,000 market value of the original 800 shares Smith exchanged in year four) and is the same as Smith would have received if he had held the original 1,000 options for the full ten years before exercising them.



### Form of Payment of Option Exercise Prices

Over the years, a number of ways have been devised to allow executives to exercise stock options without tying up their own cash.

**(i) Stock Swaps and Pyramiding.** Many plans allow payment for exercises of options to be an exchange of shares rather than cash. When a stock option plan allows payment by stock swap, the executives may exercise their options in a rapid succession of transactions which convert the difference between exercise price and market price into additional shares with no cash outlay. This practice is known as “pyramiding.” Critics argue that pyramiding undermines the goal of increasing stock ownership among executives.

**(ii) Company Loans and Grants.** Many stock option plans allow executives to pay for an option exercise with a promissory note or loan from the company, often made at below-market rates.

**(iii) Cashless Exercise.** A company may arrange for executives to make cashless exercises through a broker. Under a cashless exercise, when an executive wants to exercise an option, the broker purchases the necessary shares from the company, pays the company the exercise price of the option, and immediately sells the shares at the current market price. The profit — the difference between the exercise purchase price and the market sale price — is given to the executive after commission costs are deducted. The executive thus earns the same profit (less commissions) he would have earned if he had bought and sold the shares directly, but without having to pay any cash.

**Change in Control Provisions** Most stock option plans include provisions that allow executives to cash in their options if a change in control occurs. These provisions, designed to protect employees from financial hardship due to an unexpected change in control, may also serve as antitakeover measures because they usually increase the cost of acquiring the company when they are activated.

In general, there are three types of change-in-control provisions companies may include in their stock plans: (1) a provision in the plan that makes all outstanding options — fully vested or not — immediately exercisable if a change in control occurs; (2) a provision to pay cash for the difference between the market and exercise prices for any outstanding options at the time of a change in control; and (3) a provision lifting the restrictions on restricted stock grants and performance awards so that executives can take full possession of outstanding awards. The first provision, acceleration of vesting, is the most common.

Some plans offer limited stock appreciation rights — a feature similar to a change-in-control cash-out provision. Like a SAR, a limited stock appreciation right is granted at the time the option is granted; unlike a SAR, it is exercisable only in the event of a change in control. When exercisable, a limited stock appreciation right entitles the holder to the difference in cash between the offerer’s price and the exercise price.

**Repricing underwater options** When options are “underwater” their market price is less than the option exercise price. Underwater options continue to show up on proxy statements, although companies rarely seek shareholder approval to replace them. More often, a replacement is done without shareholder approval under the compensation committee’s general authority to set the terms of option plans and then is disclosed in the proxy statement.

Opponents of replacing underwater options argue that it is a giveaway to executives, and that other shareholders have no such protection from a falling stock price. By taking away the downside risk, opponents say, the company indicates that executives will be compensated even if the stock price falls — which may show a lack of managerial confidence in the stock and could further depress the stock price.

Supporters of repricing say that options fail to provide their original incentive of boosting company performance if they are underwater and there is no chance of their rising above water. This argument is strengthened when the drop in the stock price is industry-wide or market-wide. Another factor is the timing of the replacement. Some experts say that an option must be underwater by a substantial amount and for a period of two years or more before support for replacement should be considered. The reason being that options usually do not expire for five to ten years and the stock price may recover in the meantime.

**Omnibus stock option plans** Comprehensive or “omnibus” stock option plans authorize the use of a number of stockbased compensation vehicles. Some plans delegate so much discretion to the compensation committee on the forms and terms of awards that some shareholders have called them “blank check stock options.”

Omnibus plans usually give plan administrators a high degree of discretionary authority with respect to the granting of options. Phrases such as “other stock-based awards” are frequently added to the long list of award types available to participants. Many of the plans contain change-in-control provisions and allow discounted grants.

**Dilution** When stock options are exercised, a company’s profits and assets are spread over a larger number of shares and each shareholder’s interest in the company is diluted. Most institutional investors look at the potential dilution of the exercise of options in evaluating stock-based compensation plans and have specific dilution thresholds (ranging generally from 5% to 10%) for deciding whether to vote for or against a stock plan. Dilution is typically calculated as a percentage by dividing the number of shares reserved under an option plan by the total number of outstanding shares. For example, if a company with fifty million shares outstanding proposes a stock option plan that reserves two million shares for issue, the potential dilution from the proposed plan is 4% (which is equal to two million divided by fifty million).

In addition to diluting pre-share earnings, exercising options can shift the balance of the voting power. The dilutive effect of a stock plan on voting power is especially important at companies that have supermajority voting requirements. If, for example, a company’s charter requires an 80% supermajority vote to approve a merger and company insiders own 15% of the voting power, then a stock plan that allows executives to acquire another 5% of the outstanding shares potentially gives insiders control of the company.

**“Evergreen” Plans** “Evergreen” stock option plans have no termination date and reserve a specified, but usually low, percentage of the outstanding shares for award each year. Evergreen plans usually allow unused shares to be carried over for grant in future years. Because these plans appear to have a low level of dilution (usually 1% per year), they may appear innocuous. Shareholders may suffer, however, from “creeping dilution” created by the plans over an extended period of time.



## Appendix C

### The CERES Principles

#### Protection of the Biosphere

We will reduce and make continual progress toward eliminating the release of any substance that may cause environmental damage to the air, water, or the earth or its inhabitants. We will safeguard all habitats affected by our operations and will protect open spaces and wilderness, while preserving biodiversity.

#### Sustainable Use of Natural Resources

We will make sustainable use of renewable natural resources, such as water, soils and forests. We will conserve nonrenewable natural resources through efficient use and careful planning.

#### Reduction and Disposal of Wastes

We will reduce and where possible eliminate waste through source reduction and recycling. All waste will be handled and disposed of through safe and responsible methods.

#### Energy Conservation

We will conserve energy and improve the energy efficiency of our internal operations and of the goods and services we sell. We will make every effort to use environmentally safe and sustainable energy sources.

#### Risk Reduction

We will strive to minimize the environmental, health and safety risks to our employees and the communities in which we operate through safe technologies, facilities and operating procedures, and by being prepared for emergencies.

#### Safe Products and Services

We will reduce and where possible eliminate the use, manufacture or sale of products and services that cause environmental damage or health or safety hazards. We will inform our customers of the environmental impacts of our products or services and try to correct unsafe use.

#### Environmental Restoration

We will promptly and responsibly correct conditions we have caused that endanger health, safety or the environment. To the extent feasible, we will redress injuries we have caused to persons or damage we have caused to the environment and will restore the environment.

#### Informing the Public

We will inform in a timely manner everyone who may be affected by conditions caused by our company that might endanger health, safety or the environment. We will regularly seek advice and counsel through dialogue with persons in communities near our facilities. We will not take any action against employees for reporting dangerous incidents or conditions to management or to appropriate authorities.

**Management Commitment**

We will implement these Principles and sustain a process that ensures that the Board of Directors and Chief Executive Officer are fully informed about pertinent environmental issues and are fully responsible for environmental policy. In selecting our Board of Directors, we will consider demonstrated environmental commitment as a factor.

**Audits and Reports**

We will conduct an annual self-evaluation of our progress in implementing these Principles. We will support the timely creation of generally accepted environmental audit procedures. We will annually complete the Ceres Report, which will be made available to the public.

**Disclaimer**

These Principles establish an environmental ethic with criteria by which investors and others can assess the environmental performance of companies. Companies that endorse these Principles pledge to go voluntarily beyond the requirements of the law. The terms “may” and “might” in Principles one and eight are not meant to encompass every imaginable consequence, no matter how remote. Rather, these Principles obligate endorsers to behave as prudent persons who are not governed by conflicting interests and who possess a strong commitment to environmental excellence and to human health and safety. These Principles are not intended to create new legal liabilities, expand existing rights or obligations, waive legal defenses, or otherwise affect the legal position of any endorsing company, and are not intended to be used against an endorser in any legal proceeding for any purpose.

## Appendix D

### The MacBride Principles

The Catholic-Protestant conflict and the discrimination problems in Northern Ireland result primarily from a protracted Irish struggle for home rule. In 1921, Ireland was partitioned between the largely Catholic south, which is currently the Republic of Ireland, and the largely Protestant northeast, which is currently Northern Ireland. Northern Ireland, unlike the Republic of Ireland, remains a part of the United Kingdom. Many Catholics in Northern Ireland continue to campaign for a united Ireland and, as a result, in the years following the partition, discrimination against Catholics in Northern Ireland with respect to housing, employment, and voting rights has been a particular problem.

In response to the problems of employment discrimination in Northern Ireland, the British parliament adopted the Fair Employment (Northern Ireland) Act 1976 (the “1976 Act”). The Fair Employment Agency (FEA) was established to implement the 1976 Act. The 1976 Act was strongly criticized because it emphasized voluntary action to end discriminatory practices and enforcement action and it was concerned with eliminating only intentional discrimination. Critics also argued that the FEA had inadequate authority to require improvements in fair employment practices, that it was underfunded, and that it lacked government backing to establish a strong position in a very controversial area.

The Fair Employment (Northern Ireland) Act 1989 substantially revised the 1976 Act by shifting the emphasis from a focus on direct, intentional discrimination to indirect discrimination. The new law established a Fair Employment Commission (FEC) which replaced the FEA. The new law requires all private sector employers with more than ten (10) employees to register with the FEC and to submit annual monitoring returns to the FEC that show the religious composition of their work force by job category and by gender. Employers that find imbalances in their work forces are required, under the new law, to engage in affirmative action efforts to improve the situation.

### The MacBride Principles

#### 1. Increasing the representation of individuals from underrepresented religious groups in the work force including managerial, supervisory, administrative, clerical and technical jobs.

A work force that is severely unbalanced may indicate prima facie that full equality of opportunity is not being afforded all segments of the community in Northern Ireland. Each signatory to the MacBride Principles must make every reasonable lawful effort to increase the representation of underrepresented religious groups at all levels of its operations in Northern Ireland.

#### 2. Adequate security for the protection of minority employees both at the workplace and while traveling to and from work.

While total security can be guaranteed nowhere today in Northern Ireland, each signatory to the MacBride Principles must make reasonable good faith efforts to protect workers against intimidation and physical abuse at the workplace. Signatories must also make reasonable good faith efforts to ensure that applicants are not deterred from seeking employment because of fear for personal safety at the workplace or while traveling to and from work.

#### 3. The banning of provocative religious or political emblems from the workplace.

Each signatory to the MacBride Principles must make reasonable good faith efforts to prevent the display of provocative sectarian emblems at their plants in Northern Ireland.

4. **All job openings should be publicly advertised and special recruitment efforts should be made to attract applicant from underrepresented religious groups.**  
Signatories to the MacBride Principles must exert special efforts to attract employment applications from the sectarian community that is substantially underrepresented in the work force. This should not be construed to imply a diminution of opportunity for other applications.
5. **Layoff, recall and termination procedures should not in practice favor particular religious groupings.**  
Each signatory to the MacBride Principles must make reasonable good faith efforts to ensure that layoff, recall and termination procedures do not penalize a particular religious group disproportionately. Layoff and termination practices that involve seniority solely can result in discrimination against a particular religious group if the bulk of employees with greatest seniority are disproportionately from another religious group.
6. **The abolition of job reservations, apprenticeship restrictions, and differential employment criteria, which discriminate on the basis of religion or ethnic origin.**  
Signatories to the MacBride Principles must make reasonable good faith efforts to abolish all differential employment criteria whose effect is discrimination on the basis of religion. For example, job reservations and apprenticeship regulations that favor relatives of current or former employees can, in practice, promote religious discrimination if the company's work force has historically been disproportionately drawn from another religious group.
7. **The development of training programs that will prepare substantial numbers of current minority employees for skilled jobs, including the expansion of existing programs and the creation of new programs to train, upgrade and improve the skills of minority employees.**  
This does not imply that such programs should not be open to all members of the work force equally.
8. **The establishment of procedures to assess, identify and actively recruit minority employees with potential for further advancement.**  
This section does not imply that such procedures should not apply to all employees equally.
9. **The appointment of a senior management staff member to oversee the company's affirmative action efforts and the setting up of timetables to carry out affirmative action principles.**  
In addition to the above, each signatory to the MacBride Principles is required to report annually to an independent monitoring agency on its progress in the implementation of these principles.