

GUIDELINES FOR A LATIN AMERICAN CODE OF CORPORATE GOVERNANCE



GUIDELINES FOR A LATIN AMERICAN CODE OF CORPORATE GOVERNANCE





GUIDELINES
FOR A LATIN
AMERICAN CODE
OF CORPORATE
GOVERNANCE





GUIDELINES FOR
A LATIN AMERICAN
CODE OF **CORPORATE**
GOVERNANCE (GLACCG)

The Guidelines for a Latin American Code of Corporate Governance have been drafted within the framework of a project sponsored by CAF. The Spanish firm IAAG Consultoría & Corporate Finance, S.A. (www.iaag.com) was responsible for the project, with the participation of a working team integrated by:

Mr. Alfredo Ibargüen, Partner/Director

Mr. José Gómez-Zorrilla, Manager

Ms. María de Ibargüen Bustamante, Associate

We thank the contributions and comments made by Michael Penfold and Andres Oneto.

Depository collection number: ifi74320133501733
ISBN: 978-980-6810-93-8

Editor: CAF

This document was prepared by the Vice presidency of Development and Public Policies of CAF.

Graphic design: Gisela Vilorio

The ideas and proposals contained in this issue are the exclusive responsibility of the authors and do not reflect the official position of CAF.

The digital version of this document can be found at: <http://scioteca.caf.com>

© 2013 Corporación Andina de Fomento

All rights reserved

CAF Prologue

Capital markets in Latin American countries are still characterized by a meager level of relative development which is reflected in a low financial intricacy and an incipient stock market capitalization. This situation has become a major obstacle to increasing the region's competitiveness, as it has a direct effect on the opportunities to access larger and more efficient financing sources for production and business sector investment.

Several factors explain this behavior; among others, problems of macro-economic instability, rule of law weakness and limitations on the regulatory framework and the institutions responsible for supervising markets. However, one of the factors that has caught the most attention of financial analysts is the lack of business transparency and weak practices of good corporate governance.

The subject of Corporate Governance began gaining ground at the beginning of the 1990's, as a result of privatization processes that took place in the countries of Eastern Europe. However, it was at the beginning of this century that it received more attention and analysis from the specialized media due to the scandals that occurred in important companies in the United States and other developed countries, like the cases of Enron, Worldcom and Parmalat.

Corporate Governance may be defined as the set of formal and informal practices governing the relations between administrators and all those who invest resources in the company, mainly the shareholders and creditors. It is evident that good corporate governance practices guarantee a better use of companies' resources, help to attain more transparent accounting practices and mitigate the problems of asymmetrical information which characterize financial markets. In these circumstances, good practices are the key to companies' access to capital markets.

Conversely, the absence of good practices is revealed in many forms: flaws in the opportunity to access financial information and transparency of the disseminated information, abuse of minority shareholders, lack of independence and integrity in auditing processes, hiring unsuitable personnel to carry out the functions of a company, among others. These shortcomings prohibit companies from guaranteeing an efficient management of their resources and from taking precautions with the patrimony delivered by investors and creditors. As a result, the access of companies to capital markets is limited.

In this context – and in line with its commitment to sustainable development and regional integration – CAF has developed a program that promotes better corporate governance practices with the aim of strengthening this process on a regional level.

As part of the activities of this program, CAF presents these Guidelines for a Latin American Code of Corporate Governance, as an update of a document published in 2004. Its purpose is to present a set of basic norms that help build the foundations of good corporate

governance to companies of the region, operators of capital markets and those responsible for public policies. This document is exhaustive and applicable to a very diverse spectrum of companies; it has a dynamic character and may be enriched by suggestions and recommendations that could arise when it is put into practice.

Through this publication, CAF expects to continue providing solid support to companies in creating a true culture of good corporate governance. While this task is a long-term one, the adoption of these guidelines may turn into a significant contribution to the development of the region's capital markets and help to optimize the relations between companies and other suppliers of financial resources.

L. Enrique García
Executive President

Index

Section I. Introduction to the Guidelines for a Latin American Code of Corporate Governance (GLACCG)	11
I. INTRODUCTION	12
II. SCOPE OF APPLICATION	19
Section II. Guidelines for a Latin American Code of Corporate Governance (GLACCG)	21
I. RIGHTS AND EQUITABLE TREATMENT OF SHAREHOLDERS	22
1. Principle of Equal Treatment (Guideline n° 1)	22
2. Right to the Non-dilution of Shares in the Company's Capital (Guideline n° 2)	23
3. Encouragement of Shareholder's Participation and Information Collection (Guideline n° 3).	24
4. Takeover or Change of Control by Another Group (Guideline n° 4)	26
5. Clauses for the Submission to Arbitration (Lineamiento n° 5)	27
II. THE SHAREHOLDERS MEETING	29
1. Function and Jurisdiction (Guideline n° 6)	29
2. Regulations of the General Shareholders Meeting (Guideline n° 7)	30
3. Classes and Call for the Meeting (Guidelines n° 8, n° 9 y n° 10)	31
A. Specific obligation to summon the meeting	31
B. Time period	32
C. Media for publicizing the General Meeting Summon	32
D. Contents of the Meeting Summon Announcement	33
E. Ability to introduce subjects on the Agenda of the Meeting	33
4. Right of Shareholders to Receive Information Previous and During the Holding of the General Shareholders Meeting (Guideline n° 11)	34
5. The role of Institutional Investors (Guideline n° 12)	35
6. The quorum and the required majorities (Guideline n° 13)	36
7. Intervention of the Shareholders (Guideline n° 14)	37
8. Regulation of the Right to Vote (Guideline n° 15)	37
9. Regulation of Representation (Guideline n° 16)	38
10. Attendance of members other than the Shareholders (Guideline n° 17)	40

III. THE BOARD OF DIRECTORS.	42
1. The need to have a Board of Directors (Guideline n° 18)	43
2. Entitlement to the Board of Directors for the functions of the Definition of Strategy, Supervision, Control, Governance and Administration (Guideline n° 19)	44
3. Regulation of the Board of Directors (Guideline n° 20)	46
4. Size of the Board of Directors (Guideline n° 21)	47
5. Categories of the members of the Board of Directors (Guideline n° 22)	48
A. Categories of the Directors	48
B. Allowed Majority of External Directors on the Board of Directors	50
6. Appointment of Board Members (Guideline n° 23)	51
7. Independent External Directors (Guideline n° 24)	57
A. Appointment of External Directors	57
B. Declaration of Directors' Independence	60
8. Termination of the Appointment of the Directors (Guideline n° 25)	61
9. Regulation of the rights and duties of the Members of the Board of Directors or Administrators (Guidelines n° 26)	62
A. Duties of the Directors	62
B. Rights of the Directors	64
10. Conflicts of Interest and Related-party Transactions (Guideline n° 27)	65
A. Conflicts of Personal Interest	65
B. Conflicts of Interest due to Activities	66
C. Transactions with related parties	67
11. Directors' Compensation (Guideline n° 28)	69
A. Compensation Policy	70
B. Transparency of the Compensation	72
12. The organization of the Board of Directors (Guideline n° 29)	72
A. President or Chairman of the Board of Directors	73
B. Vice-President of the Board of Directors	75
C. Secretary of the Board of Directors	75
13. The Chief Executive Officer and the Senior Management (Guideline n° 30)	76
14. Dynamics of the Board of Directors (Guideline n° 31)	80
15. Committees of the Board of Directors (Guideline n° 32)	83
A. Auditing Committee	84
B. Nominations and Remuneration Committee	86
C. Risks Committee	87

IV. CONTROL STRUCTURE.	90
1. Control Environment (Guideline n° 33).	91
2. Risk Management (Guideline n° 34)	92
3. Internal Control System (Guideline n° 35)	94
4. Information and Disclosure of Risk Management Policies and Control Systems (Guideline n° 36)	95
5. Monitoring the control structure	
A. The Duties of internal auditing (Guideline n° 37)	96
B. The Duties of external auditing (Guideline n° 38)	97
V. TRANSPARENCY AND FINANCIAL AND NON-FINANCIAL INFORMATION	100
1. Information Disclosure Policy (Guideline n° 39)	100
2. Financial Statements (Guideline n° 40)	101
3. Information for the Markets (Guideline n° 41)	102
4. Information about shareholders´ agreements (Guideline n° 42)	103
5. Corporate Governance Annual Report (Guideline n° 43)	104
A. Information to be included in the Corporate Governance annual report.	104
VI. FINAL REFLECTIONS ON THE IMPLEMENTATION OF THE GUIDELINES	107
Section III. Reference Guide to the Guidelines	109
PREVIOUS CONSIDERATIONS	110
Section IV – Annexes of the Guidelines	119
I. Annex I – Corporate Governance for Groups	134
II. Annex II – The responsibility of financial entities in the promotion of Corporate Governance	134
A. Corporate Governance for banking entities	136
B. Banking entities as agents for the promotion of Corporate Governance to their clients	137
C. The “MESEG” methodology for the evaluation of governance risks of clients that receive financing.	139
III. Annex III – Corporate Governance in family enterprises	140
IV. Annex IV – Glossary of terms	146

Section I

INTRODUCTION
TO THE GUIDELINES
FOR A LATIN AMERICAN
CODE OF CORPORATE
GOVERNANCE
(GLACCG)

I. Introduction

Background

In 2004, CAF - Development Bank of Latin America - published the first version of the Guidelines for a Code of Corporate Governance with the collaboration of IAAG Consulting (www.iaag.com). It is available on the website of CAF's Program for Corporate Governance, at the site: <http://scioteca.caf.com>.

The first document, which was officially presented in Cartagena de Indias, along with the OECD's *White Paper on Corporate Governance* in Latin America, was subsequently revised with minor updates in 2006 and 2010.

The publication of the Guidelines in 2004 became an important milestone for corporate governance, since it was a document specifically directed towards the corporate world. Thus, it had a strong practical focus and was based on the main international codes on best practices of corporate governance at the time, fundamentally the OECD's *Principles of Corporate Governance* and other documents on corporate governance at a national level.

The pragmatic nature of the Guidelines was based on the definition of fifty-one "Measures", related to major principles of Corporate Governance. Each Measure is composed by a variable number of "Recommendations" – a total of ninety-three – regarded as the concrete and specific practices of Corporate Governance that support each Measure.

Since its first publication, the Guidelines were gradually implemented in different types of companies in the Latin American and the Caribbean region, in many cases with the support of CAF. Thanks to its solid intellectual rigor and its strong practical focus, it has contributed to strengthen corporate governance practices and its effective promotion in many companies throughout the region. Since then, the discipline of corporate governance has experienced a notable development, both on a global and regional level, providing a response to new business realities, especially after the outbreak of the global economic crisis. It made evident, among many other variables, the profound weaknesses that still existed in the effective functioning of corporate governance in many enterprises and entities.

The aftermath of the global economic crisis resulted in a revision on a global level of the regulations and legislation in different countries, as well as the publication and update of diverse documents which compiled the best practices of corporate governance. In this context, CAF believes it is appropriate to undertake the present updating of the Guidelines that involves a profound revision and update of the contents initially set forth in the Guidelines of 2004. Both from a doctrinal/academic and practical point of view, this initiative shows further proof of the importance that CAF has given, since the implementation of the first Guidelines in 2004, to the dissemination and implementation of good practices of corporate governance in all kind of companies as a key tool to increase their competitiveness and facilitate their sustainability.

In this regard, CAF has promoted the publication of different documents with a regional scope, such as the *Guidelines for a Code of Corporate Governance for SME's and Family Companies (Lineamientos para un Código de Gobierno Corporativo para las PYME y Empresas Familiares, 2011)* or the *Guidelines of Corporate Governance for State Companies (Lineamientos de Gobierno Corporativo para Empresas del Estado, 2010)* and it has supported more than forty processes for the diagnosis and implementation of practices of corporate governance in private and public companies in the region.

Framed in the context of the global crisis and its origin, many lessons have been learned from these processes of implementation. Despite the formal advances achieved in different countries, the problems regarding the adoption and above all, compliance with sound practices of corporate governance have not been solved and are not even close from being solved.

The effects of the current crisis are, thus, a further incentive to ensure that the development of corporate governance in the region will continue to be a relevant focus of attention on the part of those institutions which, by their nature and objectives, can exert an influence on the future of businesses. An example of this is the degree of influence that can be exerted by institutional investors, certain international organizations, multilateral or development banks, commercial banks and the agencies that regulate companies or the stock exchange, or even regulated sectors of the economy such as banking, insurance, energy or telecommunications.

Consequently, the objective of the current Guidelines is to provide the business community of the region with a document, based on the same pragmatic focus of the 2004 Guidelines, fully updated to the needs of companies in terms of corporate governance, and that represents once again a reference framework that companies can use to diagnose and strengthen their corporate governance practices.

Rationale for the Review

The present Guidelines do not represent a break to those initially published in 2004, but an evolution of the same, enabling the initial ones to be adapted to the latest advances in corporate governance and to respond to the current challenges in the field, justified by three main reasons:

1. The global financial crisis has made evident the convenience of updating and deepening corporate governance practices applicable to companies. Particularly, those related to financial entities bring special attention, especially with regard to risk management, remuneration schemes for the members of their boards and senior management, and the dynamics and operational practices of their Boards of Directors.
2. In many cases, regulation itself has proven to be ineffective since it has allowed for the existence of business practices that have turned out to be especially harmful for the sustainability of companies and the creation of long-term value for shareholders. In many cases, this has led to the revision of the regulations applicable in several countries, especially with regard

to voting rights, the remuneration of the Board of Directors and senior management, or the strengthening of obligations to provide full information.

3. Especially in the context of the financial crisis, behaviors that are not very ethical, but not completely unethical, have become evident in the case of administrators and managers, who have clearly put their personal interests above those of the company and of their shareholders in the medium and long-term.

Despite the business performance shown in Latin America, which has been better than that of the European or U.S. markets, the present Guidelines deal with the revision of these crucial subjects in a way that strengthens the practice of corporate governance applicable to the companies of the region and contributes to their greater sustainability. In this regard, the 2012 Guidelines for a Latin American Code of Corporate Governance have made important contributions, especially the following ones:

- The dynamics and operational tactics of Boards of Directors have been reviewed, as a key aspect in the suitable exercise of their functions.
- A whole new area related with the control structure has been developed, which deals with risk management and internal control.
- The treatment of the remuneration of the members of the Board of Directors and senior management has been dealt in a different way.
- Certain practices of Corporate Governance especially applicable to the financial sector have been included.
- An Annex on Corporate Governance for business groups, which are of increasing importance to business in the region, has been included.

From a practical point of view, the contents of the present Guidelines are likewise influenced by the practical experience acquired through their effective implementation, with the support of CAF, in all types of companies in the region, which ensures their full applicability to the corporate reality.

This revision maintains and deepens the pragmatic focus initially found in the 2004 Guidelines, but, from a formal perspective, it has also undertaken:

- The inclusion of new practices of Corporate Governance in all fields, as well as a review of those established in the 2004 Guidelines.
- A complete revision of the text, the sequential order and wording of the original Guidelines.
- The elimination of legal references, as well as footnotes included in the 2004 version that refer to the normative framework of the countries of the Andean Community of Nations (CAN, in its Spanish initials), with the aim of extending the applicability of the present document to the Latin America and the Caribbean region as a whole.
- A redefinition of the Corporate Governance areas has been accomplished for a better distribution of the proposed practices of Corporate Governance.
- The simplification of the different types of companies described in the 2004 Guidelines, for a

better adaptability to the corporate reality of the region.

- The inclusion of Annexes to develop three subjects which we consider to be especially relevant: (i) Corporate Governance in business groups; (ii) the responsibility of banking entities for the promotion of Corporate Governance in the companies of the region; and (iii) Corporate Governance in family businesses.

It is our wish and vision that this new edition of the Guidelines for a Latin American Code of Corporate Governance will once again be a reference document that satisfies the expectations of the business community and serves as an important tool for the effective promotion and improvement of Corporate Governance in the companies of the region.

Applicability

The applicability of the present Guidelines, as well as in the 2004 initial version, depends on the free and autonomous decision of the companies to which its contents are directly addressed to. However, as we remarked above, other actors classified according to their access to sources of financing, such as institutional investors, multilateral agencies, banking entities and, above all, capital markets, could make a decisive contribution to the effective promotion and real application of the Guidelines in the companies they invest in.

This document is not addressed to public agencies or the legislative bodies and regulation authorities; it is fundamentally addressed to companies. Thus, the implementation of its contents will necessarily have to be based on self-regulation and consequently, will have to be incorporated into corporate by-laws, Board of Directors' regulations or other internal norms documents considered as suitable.

Taking this into account, we point out that nothing prevents legislators or regulators from establishing legal norms to strengthen some of the Corporate Governance practices proposed herein, some of which are already found, to a greater or lesser degree, in the existing normative framework of different countries. In fact, in the present Guidelines, we mention some Corporate Governance practices that should be taken into account by the legal frameworks and their respective regulators, to make them legally binding in order to enforce some minimum standards in terms of Corporate Governance.

In this way, the regulatory and supervisory bodies of different regulated industries, among which stand out banking and stock markets due to their potential systemic impact, should be transformed into key actors. First, to promote and disseminate an understanding of good Corporate Governance practices among the entities they supervise, and second, to ensure the enforcement of the specific regulations on Corporate Governance considering their legitimate supervisory capacity and even their moral suasion capacities

This regulation should be established by the regulator, seeking an optimum balance between the most genuine corporate self-regulation, the development of tools that fit into a form of co-regula-

tion through the use of what is known as soft law— as in the case of national codes of Corporate Governance developed by public and/or private social agents, or on an international level, the recommendations of the International Organization of Securities Commissions (IOSCO), and, a set of practices of obligatory compliance on the part of companies, approved in accordance with the most traditional legislative techniques, that is, through laws or regulations.

Nevertheless and as the 2004 Guidelines noted, *“we should not forget the recommendations of the experts at the OECD, found in the White Paper for Latin America on Sound Corporate Governance, who point out that any adjustments to the regulatory framework should be done after a careful analysis of the costs and benefits of introducing new rules, in order to avoid unintended negative effects that wind up undermining the benefits sought and thwart business activity”*.

In synthesis, the Guidelines still believe that voluntary self-regulation by companies themselves is the right focus when it comes to adopting and implementing practices of Corporate Governance. The assessment markets give to the companies' Corporate Governance should help distinguish between those companies that show a sound Corporate Governance from those whose Corporate Governance is completely neutral, where they only comply with the minimal standards, and those that show a poor governance.

Nevertheless, the Guidelines also recognize that self-regulation is not completely incompatible with an active participation of regulatory and supervisory agencies on the promotion of good Corporate Governance or with the issue of an adequate regulation that employs a strong and responsible exercise of supervision – in depth and in form – of those areas and practices of Corporate Governance of mandatory compliance. For that reason, these Guidelines are meant to be a useful tool for the effective promotion of Corporate Governance by regulatory bodies among the companies within their scope of jurisdiction, in addition to specifically note a number of practices that should be incorporated into the legal framework or applicable regulation.

Recipients

These Guidelines are fundamentally addressed to companies. It is a highly practical document that aims to maximize the dissemination and real applicability of its principles in the business community. The Guidelines maintain the principle of differentiated compliance in accordance with the type of company, just as it was laid down in the 2004 version. In this sense, the Guidelines recognize that there are two major kinds of companies:

Listed companies and financial entities

Refers to all companies with capital, wholly or in part, listed on stock markets, or that are issuers of fixed income securities. Financial entities are also included in this group, considering that while some may not be listed, by the nature of their business they have to maintain the strictest level of Corporate Governance.

Non listed companies

Any other kind of company not included in the previous group.

The Guidelines establish that it would not make much sense to impose the same levels required for listed companies and financial entities to companies that are not listed or have closed capital, like family enterprises.

For this reason, the key Guidelines and Recommendations that are specifically applicable to each type of company are described establishing a more demanding level of Corporate Governance for the listed companies than to those that are not listed.

Additionally, as indicated in its Coverage of Applicability, this document presents a number of Key Guidelines and Recommendations that should be taken into consideration by legislative bodies or by agencies that regulate companies or capital markets, when issuing regulations. This should encourage mandatory compliance of the rules for companies rather than leaving it to their discretion.

The Foundations of Compliance

The Guidelines maintain the same fundamental principle found in the initial version of 2004, internationally known as “comply or explain”. By this, the companies that freely adopt these Guidelines must comply with their contents or explain which Guidelines or Recommendations they do not or only partly intend to comply with.

The information regarding the compliance with the present Guidelines and Recommendations should be revealed in the reports on Corporate Governance of each company, or in their annual reports at the end of the financial year, which should be available on the company’s website. The justification for maintaining the principle of “comply or explain” is still the same as that found in the 2004 Guidelines.

As explained, we consider that *“it is an optimum mechanism for a company to partially or completely adopt the applicable Corporate Governance Measures included in GLACCG to make the respective advances in corporate governance known to the pertinent third parties (shareholders, investors, banks, regulators, etc.).*

In second place, it is a mechanism that requires a commitment and at the same time is very flexible. It requires a commitment as both, the report on Corporate Governance and the managerial report, are corporate documents that are the exclusive responsibility of the Board of Directors. Therefore, the board must be especially rigorous about its public explanation of the degree of compliance with each of the measures of Corporate Governance.

It is flexible, since it allows the company to explain and demonstrate the actual implementation of a given measure of Corporate Governance or give a reasoned explanation for its non-compliance; either because there is an obstacle on its application in the current legislation or because the company does not agree with the contents of the measure or the convenience of its adoption”.

Structure

The present document is divided into four sections.

1. The present **Section I** is an introductory section that explains the focus and scope of application of this document.
2. **Section II** reviews the contents of the Guidelines in order to justify and explain each of the Guidelines and Recommendations applicable to the different types of companies. In this section, the contents are structured as follows:

Five large areas of Corporate Governance have been defined, which arrange the specific Guidelines and Recommendations into broad subjects:

- Rights and Equitable Treatment of Shareholders
- Shareholders Meetings
- Board of Directors
- Control structure
- Disclosure of Financial and Non-Financial Information

For each of these five areas, a number of specific guidelines have been identified as major principles of Corporate Governance from which a set of recommendations are derived. These recommendations are considered individual practices of Corporate Governance that help justify the compliance of the guideline. Each guideline will be broken down into a specific number of recommendations. At the end of each guideline a series of tables is included which, in addition to indicating the key recommendations covered by the guidelines, indicate its specific applicability according to the type of company.

3. **Section III** takes the form of a rapid reference guide summarizing the set of Guidelines and Recommendations applicable to each kind of company.
4. **Section IV** includes four annexes that deal with four subjects considered as relevant and of maximum application in the business community of the region:
 - **Annex I:** refers to Corporate Governance in the case of business groups or financial conglomerates. This annex includes a set of guidelines specifically designed for such groups that we hope will strengthen Corporate Governance in these kinds of business organizations.
 - **Annex II:** refers to the responsibilities of financial entities in the region on promoting Corporate Governance among their corporate clients, or in other words, the companies to which they provide financing to.
 - **Annex III:** refers to the particular characteristics of Corporate Governance in family enterprises.
 - **Annex IV** includes a glossary of the terms employed in the document.

II. Scope of application

Scope

Corporate Governance is not meant to be an end in itself, but one of the means that a company – private or public, listed or not – may use to facilitate the raising of financial resources at reasonable costs, better manage its managerial risks, and to become stronger and sustainable.

There is abundant literature on Corporate Governance that has inspired in many cases the development of specific norms and regulations on the subject. However, it has not resulted in a single, universal model of good Corporate Governance. Nevertheless, the absence of a universally applicable model of Corporate Governance does not imply that a series of standards cannot be considered as objectively valid reference points and applicable to companies in general, adapting them to their particular characteristics.

The present Guidelines take the contents of the 2004 Guidelines into consideration, updating them thoroughly with the aim of incorporating both the recent advances in the study of Corporate Governance and the practical vision which has resulted from their implementation in numerous companies of the region.

It is worth noting that the present document, similarly focused as the 2004 Guidelines, pays close attention to the aspects most directly related to pure Corporate Governance, and, thus, concentrates on the world of relations that exist between Ownership (the shareholders), Administration (the Board of Directors) and Management (senior managers). With this, it aims to establish a system of checks and balances or reciprocal controls that supports the efficient functioning of the company, strengthens its sustainability and allows for an adequate protection of the shareholders and other interested parties

Considering this, other issues – such as corporate ethics, the environment and corruption – are not dealt in a specific way, nor are other matters that are regarded as secondary, including topics as Corporate Social Responsibility (CSR) in the management of relations with other stakeholders (employees, creditors, suppliers, the local community and others).

Nevertheless, while there is a general consensus that to a large extent the recent financial crisis can be attributed to the shortcomings and weaknesses of Corporate Governance, it is also true, as the OECD points out, that the global crisis has been caused *“by a toxic combination of anti-ethical conducts on the part of companies and the failure to regulate and supervise their activities”*. In other words, the personal conduct of the relevant actors in important companies was marked by anti-ethical actions that could have not been spotted by the system of Corporate Governance, or, if it was, it did not lead to any kind of responsibility.

In this sense, the Guidelines, externally promote the reinforcement of the regulatory and supervisory capacities, and, internally demand the companies a vigilant attitude towards anti-ethical conducts, through the actions of the board committees and the implementation of internal complaint lines available to employees.

Implementation and Application

The Guidelines gather a series of practices of Corporate Governance that when adopted should be incorporated into the by-laws and/or internal norms of companies. Eventually, they could become rules of mandatory compliance.

For this purpose, we would define the internal norms of companies as the set of rules and normative documents of the company itself and/or its shareholders, like the by-laws or the regulations for the internal regime of the Board of Directors or the Shareholders Meetings, among other norms.

Thus, an effective implementation of the Guidelines implies the introduction of necessary, and substantial in many cases, changes in the company's operational rules.

That is why it is crucial to consider the Guidelines not only as a set of isolated practices of Corporate Governance which are to be incorporated into the internal norms of the company, but also as a whole business culture that should guide the actions and relations between Ownership, Administration and day to day Management.

Consequently, a process must be undertaken before proceeding to its formal implementation to ensure their full intellectual adoption or acceptance by the Ownership, Administration and Management of the company, defining the scope for the effective incorporation of these practices of Corporate Governance in each of the levels described.

If there does not exist enough motivation to incorporate some of the practices proposed in this document, it may even be preferable to proceed to an exclusive implementation of those practices on which there is a majority agreement before going on to the full implementation of their contents to avoid a failure to comply in practice.

In short, we understand that the process for strengthening the practices of Corporate Governance in a given company, following the contents of these Guidelines, must be a gradual one. It should implement the changes gradually allowing for better governance in the company without placing unnecessary tensions on its functions, avoiding possible adverse effects.

Finally, Corporate Governance is a dynamic reality. We understand that the Corporate Governance practices implemented by a given company will have to be subject to periodical revision. The goal is to avoid constructing a regulatory fabric considered as a "straitjacket" that may jeopardize its flexibility. The aim, instead, would be to establish a set of practices suitable to each company and allow for its most efficient functioning over time.

Section II.
GUIDELINES
FOR A LATIN
AMERICAN CODE
OF CORPORATE
GOVERNANCE

I. Rights and Equitable Treatment of Shareholders

The recognition of the rights of shareholders and the mechanisms for their implementation is one of the most important aspects, from the point of view of Corporate Governance; the shareholders, regardless of whether they own a controlling or significant share of the stocks, are the real owners of the company and those who supply the capital for the exercise of its activities.

Consequently, shareholders should (or would have to) be recognized for a series of key property rights, included in the current legislation of each country in many cases, which are usually associated with the rights to:

- Influence the company, basically through their participation and vote in the Shareholders Meetings.
- Receive and claim information.
- A share in the earnings of the company (or answer for its losses).

Given that managing a company is a complex matter that requires fast decision-making capabilities and a number of given skills, shareholders cannot be the ones who directly carry out these functions (except in very small companies) That is why they normally delegate the administration of the company to the members of the Board of Directors, who in turn delegate the day by day running of the company to the senior management by establishing three levels: Ownership, Administration and Management.

What was previously mentioned is considered as the root of the agency problem and it is the fundamental justification for Corporate Governance, which devotes its attention to the relations among Ownership, Administration and Management.

When the shareholders act solely and exclusively as such, (without being members of the Board of Directors or the senior management at the same time), they exert a series of rights centered on certain key matters of ownership like electing or dismissing members of the Board of Directors, modifying and approving the company's by-laws, receiving information about the progress of the company, the transfer of shares, and in general, a series of basic matters that in many cases are established by the legal framework and the by-laws of the company. From the standpoint of Corporate Governance, the main focus lies in the recognition of these rights, but especially in the mechanisms for their equitable exercise.

Therefore, in these Guidelines we do not attempt to present an exhaustive account of those rights, but to deal with their treatment in the most appropriate way, in order to clarify and deepen the understanding of their contents.

I.I. The Principle of Equal Treatment (Guideline no. 1)

The principle of equal treatment has traditionally been understood as one where one share amounts to one vote, so that the voting rights of each shareholder should be equivalent to his or her share in the company's capital.

However, this principle has evolved into the parity of treatment principle, and refers to the company’s obligation to give an equal treatment to all of the shareholders who stand in the same conditions. Unfortunately, this nuance of “the same conditions” is often ignored, yet it is essential for a correct understanding of this principle. It does not refer to an equality of treatment in an absolute sense, since not all of the shareholders are the same, thus, they cannot and they should not be treated as if they were.

The shareholders are not equal since their condition varies according to their circumstances and characteristics. This establishes a distinction, for example, between major and minor shareholders, those who may or may not represent a conflict of interest (real or potential) with the company, stable and temporary ones, and the most important (and perhaps the most transcendental) between those who are active and willing to influence the life of the company, and those who are passive.

Therefore, treating all of the shareholders the same, regardless of their nature, would not make sense, that is, beyond acknowledging the old principle of one share, one vote. The objective of the parity of treatment principle is to prevent shareholders that are in the same condition from being treated in a different way in their relationship with the company.

Hence, when shareholders are presented in different conditions it is perfectly legitimate to establish differences in the practices or forms of relationship with the company, as for example, in their access to information, the corresponding channels and circuits of communication, the personal relationship between the shareholders and the company and its administrators, or other matters.

For example, the experience shows that large institutional investors who own shares of non listed companies are required to sign a bilateral agreement between the company and the investor which imposes certain obligations to provide direct information on the company.

The parity of treatment principle may not justify in any case a situation where the shareholders who are closest to the company have access to privileged information enabling them to obtain advantages when it comes to making decisions about their shares, to the detriment of the rest of the shareholders.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
1. One share, one vote	✓	✓	✓
2. Differentiated relationship between shareholders and company	✓	✓	✓
3. Absence of advantages gained from privileged information	✓	✓	✓

I.2. Right to the non-dilution of shares in the company’s capital (Guideline no. 2)

There is an evident concern when there are cases of undue appropriation of the wealth created by the company by actors close to the governing bodies of the company such as those

who own a controlling or significant share of the capital, directors and members of the senior management.

In cases when the operations may affect the rights of the minority shareholders (such as in capital injections or mergers), these should be explained in detail by the Board of Directors in a prior and specific report, with the opinion of an external consultant (“fairness opinion”); the appointment of the external consultant should ideally count on the favorable vote of the independent members of the Board of Directors. These reports should be made available to the shareholders.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
4. Prior report by the Board of Directors	✓	✓	✓
5. Opinion of external consultant	✓	✓	✓
6. Publication of reports	✓	✓	✓

1.3. Encouragement of shareholder’s participation and information collection (Guideline no. 3)

Acknowledging that in practice it is impossible to run a company through an Annual General Meeting, the reality of recent business experiences has evidenced the enormous gaps in communication between the Board of Directors and all the shareholders. This means that this situation prevents or makes it difficult to the shareholders to adequately oversee their legitimate rights, both economic and political.

Therefore, going beyond the minimal legal rules in force, the company will have to establish precise channels to facilitate communication with the shareholders, by means of which the latter may demand information from the company or ask questions of interest to the company or ones which are associated with their condition as shareholders.

The first and most important channel of communication with the shareholders is the corporate website that should be mandatory for listed companies and financial entities. It should display financial and non-financial information, especially the internal norms regulating the organization and functioning of the company.

The obligation to establish a corporate website has already been incorporated into the legal framework of several countries in the world, so that a minimum number of mechanisms are established to strengthen the right to information of shareholders and investors.

We call upon the regulatory agencies of the region to require listed companies and financial entities to develop a corporate website with a user-friendly format, where certain levels of easy access information are portrayed. On the assumption that they have a wide base of shareholders, listed companies may choose to organize a specific department towards this end, for example, an Office for Shareholder Information. In the case of non listed companies, it may be sufficient to assign the job

of shareholders relations to the general secretary or an equivalent department. The shareholders will, thus, be able to ask questions and request to examine documents relevant to the management and activities of the company, and particularly, those related to all the information that the company makes public at the very moment of its publication.

Companies will then examine the questions, suggestions and comments of the shareholders, and whenever possible, either individually or in a collective manner, directly answer the shareholder in writing in the shortest possible time without claiming they cannot do so because of a lack of information or documentation that should be available.

In no case may the right to ask for and examine documents reach to those containing confidential information about the company or that has to do with industrial secrets that if divulged, may be used to harm the company. In addition, companies may organize quarterly informative meetings with the shareholders, with the aim of presenting the results of the previous quarter.

In the case of listed companies or those with a wide range of shareholders, the organization of these types of meetings may be done through the use of modern communications media, so that shareholders do not have to personally attend. In the case of non listed companies or those with a small base of shareholders, they may be face to face. In all cases, this kind of informative meetings should be led by the company’s Chief Executive Officer (CEO).

At the moment a shareholders’ meeting is announced, listed companies will incorporate into the corporate web page, with limited access only to shareholders if desired, information relative to the announcement of the call and its supplementary documentation, in addition to that it deems suitable to facilitate shareholders attendance and their active and informed participation.

Additionally, to promote the flow of communication between the listed companies and their shareholders, it is advisable that, to the extent possible, they compile a shareholders log that would enable them to open a direct and flexible channel of communication; as long as the Board of Directors establishes suitable technical and security mechanisms. While acknowledging the difficulties for these kinds of companies, it would be convenient for them to establish as an objective the identification of the shareholders responsible for “free-float” capital.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
7. Corporate website	✓		✓
8. Communication with shareholders	✓	✓	✓
9. Specific department	✓	✓	✓
10. Informative meetings	✓	✓	✓
11. Shareholders log	✓		
12. Electronic channel of communication	✓	✓	✓

I.4. Takeover or Change of Control by another Group (Guideline no. 4)

Listed companies often adapt mechanisms to protect themselves from hostile takeovers. In recent years, however, the trend has been to reduce these types of strategies. They are normally implemented through the by-laws or through agreements with the shareholders, since on many occasions these mechanisms have harmed minority shareholders who have lost the chance to sell their shares at the highest possible price.

Generally speaking, the following are some practical examples of what might be regarded as measures that listed companies take to protect themselves from takeovers:

- Requiring a director to own a minimum number of shares.
- Requiring a director to have served on the board for a minimum number of years before becoming chairman (president) of the board.
- Limiting the number of votes a shareholder may issue, independently of the number of shares he or she owns.
- Requiring a shareholder to have a certain nationality.
- Requiring a member of the board to have a certain nationality.
- Golden parachute contracts for senior executives, without knowledge of the Shareholders Meeting.

For that reason, we propose the **elimination of these types of agreements when a hostile takeover takes place**, since the company becomes more vulnerable to a takeover and thus, more attractive for many shareholders. In fact, from a good Corporate Governance perspective, the existence of special statutory rules in that field should not be allowed under any circumstances: in the form of limiting clauses and to try to prevent takeovers in practice or to favor their presentation.

The takeover regime should clearly establish the premises for a change of control of a listed company. This should be done regardless of whether such a change occurs through the acquisition of a majority shareholding. This way the major shareholder(s) would be obliged to open the takeover bid to all of the shareholders who have failed to approve or agree to that change of control, at the same price at which the share was purchased and control of the company was assumed. In the case of non listed companies we would have to add to the takeover proofing approaches, the right to preferential acquisition of old shares offered up for sale by a shareholder, or the requirement to approve the sale of a share by the rest of the shareholders or the Board of Directors.

Finally, a mechanism should be implemented to ensure an equal share-out of the “control premium” in non listed companies or in those where the shareholders with a controlling interest have withdrawn from the takeover bid. This mechanism would fall under law and shareholder agreement requirements, and would allow for a **tag along right** in favor of the other shareholders when a shareholder owns a share percentage that would lead to a change of control of the company. This right forces the controlling shareholder to offer the other shareholders the possibility

to sell the securities jointly in the same conditions, in whole or in part, depending on whether the acquisition is done through the entire social capital or parts of it.

In this sense and from the perspective of a controlling shareholder and the minority ones, it is important to take note of **situations of conflict of interest which may arise in business groups** when, regardless of whether the parent company is listed or not, a subordinate company is listed on the stock exchange. A similar problem may even arise in companies that are not listed and form part of a business group. In that situation, as a measure to protect the minority shareholders from the subordinate company, it is recommended that:

- The parent company and the subordinate one define a reference framework or, when possible, sign an agreement made public by both parties that defines the following:
 - The respective areas of activity and eventual business relations between the other companies of the group and the parent company.
 - The mechanisms aimed at solving conflicts of interest that may arise.
- When related-party transactions exist or are foreseen between a listed subordinate company and its parent company, whether its shares are quoted or not, the policy for dealing with conflicts of interest should be applied with a special sensitivity and rigor.

Given the above, in some cases, it could come to think that in the Board of Directors of the subordinate company, the combination of independent and patrimonial directors nominated by shareholders with no links with the dominant parent company can have an ample majority. This is an alternative that, while promising for handling potential conflicts of interests, could turn into an anti-takeover measure.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
13. Elimination of anti-takeover proofing	✓		
14. "Tag-along" right		✓	✓ (non listed)
15. Special handling of conflicts of interest between the parent-subordinate companies, and the minority shareholders.	✓	✓	✓

1.5. Clauses for the submission to arbitration (Guideline no. 5)

The absence of agile mechanisms to resolve internal conflicts in the heart of a company usually concerns both the shareholders and a series of interest groups (suppliers, clients, financial entities, etc.). They prefer to deal with companies that resolve these conflicts in an agile way helping their stability. In that respect, arbitration is a wonderful alternative to the administration of justice that in occasions has proven to be slow and inefficient in resolving conflicts in companies' environments.

While it is true that arbitration may be more burdensome in economic terms than common judicial mechanisms, we believe that in many cases it is much more convenient since it allows for a quicker solution to the disputes that eventually may arise in a company.

Evidently, certain corporate disputes, by law, must be submitted to the jurisdiction of the courts, but that should not affect the general validity of resolving such disputes through arbitration in most cases.

From the practical point of view, usually three problems may arise fairly often: (i) the implementation of arbitration is not backed by an adequate regulation; (ii) the procedures may turn out to be cumbersome and (iii) a possible abuse of the appeal for annulment of the arbitral award may arise.

Even though these risks exist, it does not seem they invalidate arbitration as the best mean to resolve controversies at the heart of a company.

That is why we believe that companies should adopt **arbitration clauses which commit them to submit to arbitration** to resolve controversies resulting from the Board of Directors' or senior management's failure to comply with the internal norms.

The arbitration clause should be established for any dispute between the shareholders and the company that has to do with relations between the shareholders and the Board of Directors or challenges the agreements made by the General Meeting and the Board. It should also demand the submission of the directors to an institutional or administrative arbitration, in no case ad hoc, undertaken by an independent institution, with the aim of establishing a framework for the resolution of any disputes that may arise in a reasonably timely, effective and trustworthy manner.

Considering the scope of the conflicts that may be submitted, the possible limitations of the national legislations in the region may place on arbitration should not be forgotten, insofar as there are certain matters that can be only be settled by the legal or even an administrative authority.

KEY RECOMMENDATIONS	Recipients		
	Listed	Non Listed	Financial Entities
16. Arbitration clauses with a commitment to submit to arbitration.	✓	✓	✓

II. The Shareholders Meeting

The Annual General Meeting is the supreme and sovereign body of a company. It groups the shareholders together constituted in the Annual General Meeting and exercise in a collegiate form the powers which correspond to the shareholders, many of which are recognized by the law, and in many occasions, intended by the company's own by-laws.

However, in line with the three levels of Ownership, Administration and Management, it might be said that the key power of the Annual General Meeting is its effective capacity to control the progress of the company and thus, of the actions of the Board of Directors.

The control of the responsibilities the shareholders delegate to the members of the board takes place at the Annual General Meeting, as it constitutes the body that gathers together all the owners of the company and where the interests of the company are manifested.

The reality is that despite its crucial importance and the great importance of its powers, the Annual General Meeting is a body that in many occasions is weakened by its own formalism and lack of agility. This situation becomes even more critical when referring to the General Assemblies of Shareholders of companies listed on public stock exchanges. In this case, the existence of many shareholders who are individual investors (and only supply capital), instead of those who are truly committed to the company, has led to the steady weakening of the active role of the Annual General Meeting as a key body. In the face of this reality, we present a set of measures that through good Corporate Governance seek to revitalize the role of the Annual General Meeting as the governing body and of effective control of the administrators, so that the shareholders may change from a state of "shareholder apathy" to a state of "shareholder activism".

These types of measures are strongly linked with the promotion of new technologies in the corporate world that maximize access to information, the existing channels of communication between the company and its shareholders, mechanisms for exercising their vote or representation, or the grouping of shareholders.

II.1. Function and Jurisdiction (Guideline no. 6)

The commercial legislation of the countries in the region recognizes the Annual General Meeting as the sovereign and supreme body of the company. The reality is that, despite its crucial importance, the Annual General Meeting is a body that in many occasions is weak. This is fundamentally due to its formalism and little agility that has caused many to question its existence as a governing body.

For that reason, we understand that the by-laws must clearly assign the meeting all the fundamental functions for governing the company, the power to adopt all types of agreements about its governance and in general, all the measures that ensure compliance with the by-laws and common interests of its shareholders.

Among the **exclusive and non-delegable faculties** which will be attributed to it will include the power to: (i) approve the annual accounts; (ii) approve the governance of the Board of Directors

and its proposals for the distribution of earnings; (iii) appoint and remove the members of the Board of Directors, (iv) appoint the external auditors; (v) approve the general policy for remunerating the Board of Directors; (vi) decide on the sale or use as collateral of strategic assets essential for the development of the company's activities; (vii) approve the policy for treasury stock or buy-back of its own shares and (viii) approve mergers or divisions of the company and the transformation of the company into a holding company by setting up subsidiaries or incorporating subsidiary entities for essential activities hitherto undertaken by the company itself.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
17. Recognition of exclusive and non-delegable powers	✓	✓	✓

II.2. Regulations of the General Shareholders Meetings (Guideline no. 7)

Listed companies should have **rules of procedure for the General Shareholders Meetings**. It is very important to define in a document the role of the General Shareholders Meeting as it acts as the basic decision-making and controlling body of the company's life, and guardian of the interests of the shareholders.

This document should cover all the matters related to the General Shareholders Meeting, including the summons, its preparation, information of those involved, the participants, format and the exercise of the political rights of the shareholders.

This way the shareholders are completely informed about the regime which governs the running of the meeting and the company will minimize the possibility that shareholders will fail to attend because of a simple lack of knowledge on how to exercise their rights.

It is equally advisable that other companies with a wide base of shareholders, regardless their shares are quoted or not on a stock exchange, approve a set of rules for the meeting, following the suggestions set forth in this section. The rules should be approved by a simple majority vote of the shareholders, usually following a proposal of the Board of Directors, which may also propose modifications.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
18. Regulations for the Meeting	✓		

II.3. Classes and Call for the Meeting (Guidelines no. 8, no. 9 and no.10)

A. Specific obligation to summon the Meeting

The Annual General Meeting should be held within the term set by the by-laws, which should never be later than the three first months of the year following the end of the financial year. Unless otherwise specified, the by-laws may set a specific date and time for the Annual General Meeting at the registered office or main office of the company. The shareholders must be informed of any restrictions on attendance.

Provided that matters of interest to the company justify it, the Board of Directors will have the power to call an Extraordinary General Meeting. In addition, and necessarily, an Extraordinary General Meeting should be summoned when shareholders who have a significant share in the company's social capital call for it.

In our opinion, in the case of listed companies the **calling of an Extraordinary General Meeting at the demand of the shareholders** should take place when a plural number of shareholders, who represent a minimum of 10 % of the social capital, request it. For other companies, it is only required to comply with the criterion of a minimum percentage of social capital.

The two criteria required in the case of listed companies -a number of shareholders and a certain percentage of represented social capital- aims to ensure that the interest in the meeting is not only that of a single shareholder but of a certain number of shareholders in the company.

In terms of setting a plural number -determining how many shareholders are necessary-, it would be hazardous to establish a universal rule for all kinds of listed companies or financial entities, given the important differences in their capital structure.

For that reason, fixing a plural number, along with the requirement that at least 10% of the social capital is represented, turns out to be a valid proposal; as it allows in practice for the strengthening of the exercise of this right, and at the same time it protects the company from an abusive or unjustified use of that right.

Regarding the required percentage of capital, while it is true that the majority of the legislations normally establish a percentage of 25% of the social capital to summon an obligatory Extraordinary General Meeting, it may be very difficult to reach this percentage. Especially if the capital is very widely distributed among different shareholders, it requires significant organization to attain the percentage set by law.

Hence, we believe that setting a lower percentage of around 10% would clearly help to improve the legal guidelines and provide a more effective possibility to shareholders to exercise this right. It would be more consistent with the company's capital structure and in the end, stricter for the Board of Directors, and more favorable for the shareholders.

The Board of Directors must summon an Extraordinary General Meeting within a reasonable period. It should not be longer than thirty days and should respect the agenda proposed by those who called for it.

B. Time period

In recent years, everything seems to indicate that a large number of companies are actively promoting a higher attendance at shareholders' assembly; there appears to be a general acceptance of the principle that the more shareholders attend the assembly, the stronger their support will be for the Board of Directors. Nevertheless, one of the factors working against this principle is the short time that elapses between the calling and the holding of the assembly.

The Board of Directors should summon the meeting with **sufficient notice in advance** and in accordance with the period set by the by-laws; it should establish minimum periods for the publication and dissemination of the announcement of summons that are longer than those legally required.

In any case, we believe that the by-laws should establish a period of at least fifteen calendar days, from the announcement of the summons of the General Meeting. However, even in certain legal frameworks, this period is regarded as insufficient. For example, in European countries a period of twenty-one days may even be required before the date set for holding the assembly.

In short, what is intended with this practice of Corporate Governance is to avoid fixing excessively short periods for calling for the General Meeting. This is the foundation of this principle as it can cause difficulty in making awareness to the shareholder of the holding of the General Meeting or in casting his or her vote in an informed manner. Likewise, it should not be forgotten that the importance of the meetings will be determined by the subjects it deals with, and by the same token the difficulty of understanding or modifying the documents in the agenda of the General Meeting is not always the same. These considerations should be taken into account by the Board of Directors when they set the time period for calling for a meeting.

C. Media for publicizing the General Meeting Summon

In addition to the means laid down by the law, the company should try to **divulge and publicize the summon of the meeting as widely as possible**. Also, as indicated above, it should employ not only the traditional media, but also electronic media (e mail, news alert service, the corporate website and even social networks, among others).

It is no longer a secret that in a free market era, listed companies and investors are often found in different countries, and the use of digital instead of print media is becoming more frequent. Thus, the simple publication of the announcement of the assembly in a printed medium in the place where the company is headquartered is insufficient.

The Board of Directors should value the importance of the matters to be dealt with in the assembly and ensure the widest dissemination of its announcements when the subjects to be discussed and eventually approved are especially important for the company. For that reason, incorporating new technologies into the scope of the relationship between a company and its shareholders is truly crucial since it maximizes the possibility of the communication that exists between the two while minimizing its cost.

D. Contents of the Meeting Summon Announcement

The announcement of the Meeting Summon will fix the date, place and time of the meeting, the agenda of the day of the meeting and the **proposals to be agreed on**, as well as the way and place in which the documentation about the proposals is made available to the shareholders. The proposals to be agreed on should be related to the items on the agenda, submitted to vote and ideally include the Board of Director's recommendation to the shareholders on how to vote.

The legislation and regulations applicable to listed companies and financial entities should specify that the inclusion of the proposals to be agreed upon in the announcement of the convocation is of obligatory compliance. This way the Board of Directors will be forced to explain its position on the different matters on the agenda of the meeting to the shareholders, strengthening the shareholders' right to information. It also helps, in a complementary form, to minimize the harmful effects of leaving all the decision-making to the board that is what is usually done nowadays as will be explained later in this document.

The announcement must be drafted in a way that makes it understandable to any shareholder and sufficiently aware of the issues the meeting will address. Towards that end, the agenda should have a precise account of the subjects to be dealt with and abstain from hiding or masking matters of importance with an imprecise wording that is generic, too general or too broad, such as "other matters".

The items on the agenda should be detailed for their better understanding and to make it possible that each one is discussed separately at the meeting. In this way it should facilitate its analysis and avoid voting on blocks of items or proposals to be agreed on, when they should be resolved separately.

In the case of modifications of the by-laws, each article or group of articles that represent substantial changes should be voted on separately. In any case, an article shall be voted on separately during the meeting at the request of a shareholder who represents a minimum of, for example, between 5% and 10% of the social capital.

Once again, the legislator and the regulator should endorse the obligatory recognition of this right for shareholders, so that the specific contents of the by-laws win the widest possible acceptance from the shareholders as a whole. In a case where the law grants shareholders the right to withdraw or separate proposals, the announcement of the summons should expressly mention it with reference to the legal norm that establishes it.

E. Ability to introduce subjects on the Agenda of the Meeting

The call and holding of a shareholders meeting is an event that implies costs for the company, both in strictly economic terms and the use of resources (human, technological, etc.), as well a significant investment of time on all levels of the organization. Consequently, it should strive to maximize the advantages offered by each Annual General Meeting, through the inclusion of the

greatest possible number of matters to be discussed, so that there is no need to hold several meetings in a single financial year.

The aim of this practice is to make it easier for the shareholders to take advantage of the meeting summons to introduce concrete subjects so there is no need to call a new assembly within a short time. Therefore, the by-laws should recognize the shareholders' right to propose, within a reasonable limit, the introduction of new items to be debated or proposals to be agreed on the agenda.

To ensure the exercise of this right is done pragmatically, we recommend that the rules should stipulate that the Board of Directors will be obliged to respond to those requests only when supported by a minimum percentage of between 5% and 10% of the social capital, set by each company depending on ownership concentration. In cases when the Board of Directors rejects a request supported by a share of capital entitled to do so, it must present in writing the reasons which led to the rejection or invalidity of the request.

KEY RECOMMENDATIONS	Recipients		
	Listed	Non Listed	Financial Entities
19. Calling for an Extraordinary General Meeting by Shareholders	✓	✓	✓
20. Sufficient notice in advance	✓	✓	✓
21. Publicizing the Summons	✓	✓	✓
22. Proposals to be agreed on	✓	✓	✓
23. Detailing items on the Agenda	✓	✓	✓
24. Independent voting on the modification of articles in the by-laws	✓	✓	✓
25. Introduction of items on the agenda	✓	✓	✓

II.4. Right of the shareholders to receive information previous and during the holding of the General Shareholders Meeting (Guideline no. 11)

This principle of information transparency should be instilled into the relations of the company with the shareholders. This way the exercise of the right to information may only be qualified or modulated because of confidentiality or irrelevance issues of the information requested. While this principle of transparency should be respected in all of the company's daily activities, its maximum development and application should be found in its relations with the Annual General Meeting, as we noted above.

Companies should go beyond the limitations most trade laws place on the shareholders' right to information. The main issue is recognizing the right of the shareholders to consult the documents about the items on the agenda of the General Meeting in the company's offices on certain days, at certain hours, and under certain conditions. In this sense, the focus of Corporate Governance should be that "the

information goes to the shareholders and not that the shareholders have to go to the information". Thus, companies, whether listed, not listed or financial ones, should make use of electronic communications media to ensure that the documents reach the scope of the shareholders.

Additionally, the by-laws should give sufficient notice in advance about the holding of the assembly, which will depend on the contents and size of the requested information. The shareholders may **ask for such information or clarifications, when they believe it is necessary**, through traditional channels and/or new technologies. They can also submit relevant questions in writing about the matters listed on the agenda, the documentation they have received, or the public information provided by the company.

The requested information may be withheld when it is unreasonable, confidential or irrelevant to the operation or interests of the company, including privileged information of stock markets, industrial secrets or unfolding operations. In such case, the favorable outcome for the company largely depends on secret negotiations and others that may present an imminent threat to the company's competitiveness if publicized.

The by-laws should establish that when certain information is requested by a significant percentage of the company's capital, the Board of Directors cannot refuse to provide it.

The decision about what constitutes a significant percentage will depend on the shareholding structure of the company, although we believe it should not be higher than 25% of the social capital

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
26. Right to receive documentation and written information in advance.	✓	✓	✓
27. Right to request additional information and clarifications	✓	✓	✓

II.5. The role of institutional investors (Guideline no. 12)

The role of institutional shareholders is fundamental for the development of Corporate Governance. In concrete terms, the institutional investors in the region seem to be inactive, compared with more developed capital markets, where they appear to play a role of extraordinary importance in getting companies to adopt the criteria and general principles of good Corporate Governance.

This role might be played by demanding the issuers of the securities to comply with the standards of Corporate Governance. They could also insist, for example, on the election of truly independent members of the Board of Directors or handling transactions with related actors, when joining the Board of Directors and when acting exclusively as a shareholder when these kinds of transactions come under the consideration of the Annual General Meeting.

It seems especially important that the legal framework of the countries in the region deals adequately with the different kinds of institutional investors, and supervises their role and the regime of their participation in capital markets. This is particularly relevant, in the companies they invest in, when regulating the exercise of their political rights and their participation in the governing bodies of these companies. It is evident that institutional investors, whose role in the region and also in other countries has been too passive, should be persuaded to exercise their ownership rights in a more active and informed way.

Even if institutional investors have no nominee directors on the board, they should take a more active part in the formation of the corporate will; listed companies should provide them with the **opportunity to use the corporate website to publicly explain their policy for participating in the General Meeting and the reasons for their vote on each item on the agenda or the proposals to be agreed on.**

Additionally, the legislator and regulator should require with obligatory compliance that the minutes of the General Meeting specifically record how the institutional investors vote on the items of the agenda. In this sense, the flow of communication between the company and its shareholders and institutional investors will turn into a crucial aspect of Corporate Governance.

The norms applicable to investment or pension funds are of quantitative importance and provide stability to a company's capital. That is why they should include the assertion that the company administering the fund is obliged to exercise all of the political rights; especially they should include the right to attend and vote in general meetings of the securities that form the portfolio that benefits their shareholders.

In any case, management companies should inform shareholders about the policy for exerting the political rights in the companies they invest in, and leave a record of that policy in the informative documents they issue.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
28. Divulging how institutional investors vote	✓	✓	✓

II.6. The quorum and the required majorities (Guideline no. 13)

The valid adoption of agreements requires that they will be made with the support of a simple majority, procedure most frequently stipulated by the different trade laws.

There are reasons which doubtlessly justify the need to implement **higher degrees of quorum** in the meeting votations, especially when the General Meeting has been called for the second time or when adopting agreements especially important for the company's future. Among these, it is worth highlighting the fixing of a special quorum for agreements for the sale or use of the strategic assets of the com-

pany as collaterals, as well as in the case of mergers, divisions and other kinds of corporate operations that, due to their characteristics, may significantly affect the rights of the minority shareholders.

For the adoption of these kinds of agreements, high levels of support would be convenient; it should not be such that it makes their adoption impossible, by granting hidden veto rights to an indeterminate number of minority shareholders. For that reason the quorum needed to approve the agreement must be set in a range of between 60% - 70% of the social capital of the company, depending on its capital structure. Any quorum that reinforced differently from what is laid down in the law must be made known to the shareholders and, of course, incorporated into the by-laws of the company.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
29. Broad support for strategic operations	✓	✓	✓

II.7. Intervention of the Shareholders (Guideline no. 14)

Currently, most of the legislations recognize the right of shareholders to intervene and ask questions during the unfolding of the meeting. However, they should be exclusively limited to matters included on the agenda.

Nevertheless, we believe it is necessary that the legislation and the by-laws of the company expressly require the right of the shareholders to request in the meeting to **dismiss members of the Board of Directors or call them to account for failures to comply with their responsibilities**, without necessarily including it in meeting's agenda beforehand.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
30. Dismissal of members of the board or sanctions for their failure to exercise their responsibilities	✓	✓	✓

II.8. Regulation of the Right to Vote (Guideline no. 15)

The cost of a shareholder's participation in the assembly in some cases is very high, which makes it difficult for them to attend the general meeting. This occurs, for example, in the case of foreign investors who do not reside in the country where the company is headquartered; the presence of these actors is more and more frequent in the region's capital markets.

Companies should try to reduce that cost as far as possible, promoting before governments and regulators the development of technologically-secure mechanisms. These mechanisms minimize the risks of error and fraud in the use of **electronic voting** and count as present in the General

Meeting those shareholders who cast their vote from a distance.

Additionally, companies should allow for the **splitting of votes**, so that the financial intermediaries that are regarded as legitimate shareholders, but act on behalf of different clients, may vote in accordance with the instructions of such clients.

Taking this into consideration, we believe legislators should incorporate into their norms the possibility of splitting the vote for these kinds of financial intermediaries, since it would enable the company's social interest to be structured better. Finally, the by-laws should recognize the temporarily or permanently **cumulative voting** as a legitimate alternative for the exercise of such political rights as voting in the assembly through a single representative or even the possibility of nominating a candidate for the Board of Directors to represent the shareholders grouped together.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
31. Promotion of electronic voting	✓	✓	✓
32. Dividing the vote of financial intermediaries	✓	✓	✓
33. Grouping together shareholders	✓	✓	✓

II.9. Regulation of Representation (Guideline no. 16)

In general, the by-laws and rules of the general meetings in any kind of company should facilitate the opportunity for any shareholder with a right to participate in the meeting to be represented by the person he or she freely appoints, whether that person is a shareholder or not.

For that reason, and when it is not possible to implement remote voting, companies should establish simple and safe mechanisms that enable shareholders, whether physical persons or legal entities, to delegate their representation. Ideally, this would ensure that the vote made by the representatives is in accordance with the instructions received from the nominal owner of the shares.

When the Assembly is called, it is recommended that the companies publish on their corporate website or send their shareholders, **a model of a standard letter of representation**. This would include the agenda and the proposals that will be submitted for vote. The letter should clearly stipulate that if for any reason, a shareholder cannot attend the assembly and wishes to be represented by a third-party, they may do so by indicating who the representative would be, and the way he or she shall vote on each of the proposals of the agenda. In fact, a shareholder who does not give precise instructions on his vote could show that is not very interested on how that vote is cast.

Consequently, if the vote is delegated to a person who is not an administrator or employee of the company, freely chosen by the person who delegates it, but the document authorizing its delegation does not contain precise instructions about the way he or she wants his or her vote to be cast, it would nevertheless be accepted as valid.

However, it is important to alert people about a very widespread practice which we regard as particularly harmful, that consists in delegating the right to vote blank or without instructions to members of the board, senior management or the depositary institutions; in other words, delegating his or her vote, the shareholder entirely leaves the casting of the vote to his or her representative. This practice should be eradicated, instead of being encouraged, even if it presents some practical problems.

If a shareholder on his or her own initiative sends a document of delegation to an administrator or employee of the company, or the delegation arises from a public request by the Board of Directors, its individual members or from senior management, the document of delegation should follow certain requisites of transparency and definitely include instructions from the represented person about how to vote on each of the proposals to be agreed on.

The company should reject any delegation of blank votes which may be used freely and lack instructions to the board in the name of its president, the members of the board and members of the senior management of the company, and inform the concerned shareholder of the situation.

In addition, it would be desirable that the administrators of the company do not accept or ask for representations when there are topics on the agenda of the meeting where the administrator may have a conflict of interest. This may occur when the voting involves letting go administrators, or sanctions against them for not fulfilling their responsibilities or to a related transaction in which the administrator or parties linked to him have a special interest.

Regarding the delegation of votes to the charges mentioned above, whose validity depends on precise instructions on how to vote, whenever the president of the board acts as the president of the Annual General Meeting and it is he who supervises the representation of the shareholders, he should inform the meeting about the number of representations he holds, the number of shares represented and the way he or she votes. The same principle should apply when other members of the board or of the senior management of the company vote as representatives of shareholders.

Considering this, we are aware that several legislations in the region forbid the delegation of votes to the board or the members of the board, and to the administrators of the company with or without instructions. This absolute prohibition presents a further obstacle to the shareholders' participation in the General Meeting, even in an indirect form and through representation, since they have to name a third party to represent them, regardless it is a shareholder or not.

We consider that in countries where possible, the administrators should be able to receive delegated votes from the shareholders, provided that the delegator's letter of representation precisely indicates how his vote should be cast for each proposal to be agreed on. Furthermore, the regulation of the delegated vote affects the use of the vote of certain shareholders who are also administrators of the company as they are directors or members of the senior management of the company.

With the aim of preventing possible conflicts of interest, different laws in the region prohibit or limit the administrators in their condition of shareholders, to exercise their own voting rights in the assembly. In some cases, this prohibition may result in situations that might be termed artificial. For example, when the financial statements are presented to Board of Directors for their approval at the end of the fiscal year, the directors, who are also shareholders, will have to identify and instruct third parties to represent them with affirmative vote to prevent the rejection of the financial statements or approved with minority support.

We believe that the administrators who are also shareholders should be able to exert their own voting rights on any matter, except those personal ones that could present a conflict of interest. Taking this into account, it is evident that the administrators who are also shareholders should not vote or delegate their vote to representatives for matters in which they have a personal interest. For example, dismissing or sanctioning them for failing to fulfill their responsibilities or a related operation in which the administrator or the related parties have a personal interest.

Finally, if the Board of Directors formally asks the shareholders for their representation for casting a vote in the assembly, the request should indicate how the vote will be carried on. This way the delegating shareholder may adhere to the board's recommendation or indicate a vote in the opposite sense.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
34. Standard model of letter of representation	✓	✓	✓
35. Reject the delegation of blank votes to the administrators	✓	✓	✓
36. Reject representation by administrators who may enter into a conflict of interest	✓	✓	✓
37. Possibility of the administrators to accept representation when there are instructions of how to vote	✓	✓	✓
38. Exercise of the vote by directors who are shareholders.	✓	✓	✓

II.10. Attendance of members other than the shareholders (Guideline no. 17)

In line with the current trend towards revitalizing the role of the General Meeting in building the company's will and turning it into a much more dynamic body, we believe that in the case of listed companies and financial entities, the **members of the Board of Directors, and especially the presidents of the committees should attend the meeting**, except when they have a valid excuse presented to the president. Nevertheless, their inability to attend should not affect the validity of the holding of the General Meeting.

The president of the General Meeting will have the right to authorize the attendance of any other person he deems convenient, even though the meeting could revoke that authorization.

Regardless of the kind of company, it is imperative that the **Chief Executive Officer** informs the assembly about the progress of the social affairs so his/her assistance is imperative. Finally, the auditor; the presidents of the Auditing, Nomination & Remuneration, and Risks Committees , and the main executives should attend the meeting, to provide maximum information and clarification to the shareholders.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
39. Attendance of external consultants, senior management and members of the board	✓		✓
40. Attendance of the Chief Executive Officer	✓	✓	✓
41. Report of the Chief Executive Officer	✓	✓	✓

III. The Board of Directors

The Board of Directors is the key administrative body of any company, with broad responsibility for the exercise of the functions of strategic guidance, supervision, control administration and arrangement of day to day management, usually delegated to the senior management. The suitability of the Board of Directors as an administrative body, compared to other alternatives, is based on its collegiate nature and the dynamics of its meetings. It is also the body that can best represent the capital structure of the company.

The Board of Directors has gone through a significant evolution: from a body almost exclusively controlled by the senior management and charged with supervising specific matters, to a body that plays a key role in defining the strategic orientation of the company and is responsible for functions of supervision and control.

Once the strategic orientation of the company is defined, the Board of Directors delegates its practical execution to the senior management. Senior Management is controlled by the Board of Directors and they render accounts to the shareholders, who are the true owners of the company.

To resume, the key functions of the Board of Directors include:

- Definition of strategies
- Control of the senior management
- Supervision of the company

However, the formal recognition of these functions does not necessarily imply their correct implementation; they may affect both the company's creation of value, and especially, an adequate protection of its shareholders. For that reason, on the perspective of Corporate Governance and of these Guidelines, a great deal of attention should be paid to the Board of Directors.

Thus, these Guidelines deal with aspects ranging from the composition, structure, formation, nomination and dismissal of members of the Board of Directors to their functions, rights, duties, dynamics and training, with the aim of helping to create active and sufficiently empowered Boards of Directors that develop the critical functions that correspond to the best governance of any company.

In short, the aim is to prevent the existence of boards that tend towards co-administration and interfere with aspects pertaining to senior management, or boards that might be hostages to the senior management: both situations are harmful as they reduce the value this body should actually have.

The final objective, from the standpoint of Corporate Governance, is to establish Boards of Directors with a clear separation of powers between the work of the senior management and that of the Board of Directors itself. The members should have the profiles needed to contribute to the well-being of the company, and guided by a clear willingness to turn the board into the key body of governance, engage in open discussions and debates, analyze all aspects in depth and freely express their reasoned opinions.

III.1. The need to have a Board of Directors (Guideline no. 18)

Given the wide variety of companies to which the Guidelines are addressed, we grant that the administration of a company may be adjusted to its specific nature. This would allow for different variants of the administrative bodies, as for instance, a single administrator; several administrators who work in a joint or associated manner; or a Board of Directors.

Nevertheless, we believe that one of the fundamental rules that should be taken into account from the point of view of good Corporate Governance, is that commercial companies should count on a collegiate-type body as its Board of Directors, one with a defined structure and a size corresponding to the dimensions and governance needs of that company. Thus, as a general principle, the companies that adopt these Guidelines, regardless of their kind, **should have a Board of Directors with a number of members sufficient to adequately perform its functions.**

While some schemes for administering companies are different to that of the Board of Directors, they are fully valid for certain kinds of companies. The advantages for companies that assume the board as the body of administration is universally acknowledged nowadays. Especially those regulated and subject to supervision and those that rely on capital markets and in general external sources of finance are exerting a stronger and stronger pressure to secure greater efficiency in the way that companies are run.

Therefore, among the advantages of having a Board of Directors as the administrative body of a corporation is that it takes different points of views and opinions into account. This happens because of the deliberative nature of the board, the professional character of its work, the company’s need to accommodate a variety of shareholders, the institutional structure that adapts it to generational changes, the collegiate manner with which it makes decisions and of course, its increasingly formal and professional structure.

The establishment of a board implies the need to deal with complex matters involving its organization, composition, size, creation of committees and definition of its functions and powers, etc. However, the advantages of a collegiate corporate administration overseen by a Board of Directors compensate, in large measure, for the difficulties involved in creating it.

It is desirable that the composition of the members of the Board of **Directors maintains certain symmetry with the company’s shareholding structure.**

KEY RECOMMENDATIONS	Recipients		
	Listed	Non Listed	Financial Entities
42. Need for a Board of Directors	✓	✓	✓
43. Symmetry with the company’s shareholding structure	✓	✓	✓

III.2. Entitlement to the Board of Directors for the functions of the Definition of Strategy, Supervision, Control, Governance and Administration (Guideline no. 19)

The by-laws should clearly define the mission of the Board of Directors and those functions that clearly cannot be delegated. Except for matters of exclusive jurisdiction of the Shareholders' General Meeting, the Board of Directors is the maximum body of administration of the company; it involves its representation, the running of business affairs and executing any activities needed to attain its social purpose.

Instead of giving a long and detailed account of the powers of the Board of Directors, it is preferable to explain that in terms of good Corporate Governance, the Board of Directors must fully understand what its general functions should be and that they are exerted, on a practical level, as a set of powers and responsibilities. In this sense, the general functions of the Board of Directors include: **defining the strategy of the company, supervising** a series of specific matters, **controlling the management and governing** the company.

In addition, it is understood that as the maximum body of administration of the company, the Board of Directors has full powers to approve the disposition of goods or to give instructions about any kind of operation necessary to fulfill the company's social purpose. Another aspect is that in normal conditions, a progressive Board of Directors tends to delegate the day to day management of the company to the executive bodies and the management team led by the Chief Executive Officer, so that it may focus its attention on the general functions previously mentioned.

Defining the strategy of the company should respond to the question *where do we want the company to go in the medium term?* Without a doubt, this is a key function of the Board of Directors. Under no circumstances the board may delegate this function to the senior management, regardless it receives its main inputs on the company's business and the environment in which it undertakes its operations from the senior management.

It is undeniable that the Board of Directors cannot fail to **monitor** a series of matters that if not adequately administered, may negatively affect the company as a whole.

Aspects like the control structure, that includes control environment, risks, internal control, information and evaluation, monitoring (auditing), conflicts of interest, transactions with linked parties, the quality of internal and external information, human resources, succession, corporate ethics and other critical matters that must not be ignored by the Board of Directors. Consequently, it must know what is happening in the company and monitor or oversee its activities. In any case and when it corresponds to the board, it must provide the needed resources and also insist that the executive body manages them adequately.

Depending on the size and complexity of the company and the specific matters supervised by the Board of Directors, this function should be directly undertaken by the board or it should call on the support of some of the board's committees. The presence of true external independent directors will help the board to come up with a rigorous and independent analysis of the situations that may

arise. This is something that is especially needed in sensitive matters such as conflicts of interest, transactions with linked parties, salaries and corporate ethics.

A Board of Directors that is not involved in the day to day management of the business is not seeking to co-administer the company, but may maintain the right to approve certain operations that are strategic, extraordinary or of great volume or complexity, delegating the day to day management of the company to the senior management, led by the Chief Executive Officer. This way of acting evidently justifies and demands that the Board of Directors exert a systematic **control** over the activities of the senior management, and by extension, of the performance of the company.

Finally, the Board of Directors serves as a link between the ownership, represented by the shareholders, and the day to day management, represented by the Chief Executive Officer. Thus, it must take the lead in the development and implementation of a model of **governance** that fits in with the nature and characteristics of the company.

The model should be structured in the form of a system of “checks and balances” between three levels: ownership, administration and management. Thus, it facilitates an alignment of the interests of the different actors that without a doubt will strengthen the trustworthiness of the company and, in the end, the value creation for the shareholders.

Based on this, the internal norms should establish a number of **powers that will never be subject to delegation**, such as the following:

- a) The approval and monitoring of the corporate strategy, annual budgets and business plan.
- b) The approval, and when appropriate, the proposal of the general policies of the company to the Annual General Meeting.
- c) The definition of the structure of the company and/or business group and its structure of finance and investment.
- d) Guarantying that the process for nominating and electing the directors is formal and transparent.
- e) The appointment, remuneration, evaluation and termination of the Chief Executive Officer.
- f) The approval of the general policy of remuneration and evaluation of the senior management.
- g) The appointment, following the proposal of the Chief Executive Officer, of salaries, and in some instances, dismissal of the senior executives of the company as well as their compensation clauses.
- h) The control of the performance and day to day management of the senior executives, as well as their evaluation.
- i) Determining the main risks to the company, including those in off-balance sheet operations and especially establishing suitable follow-up systems of internal control, including off shore operations; they should be undertaken in accordance with the procedures, systems for risks control and early warning signals approved by the Board of Directors.

- j) The integrity and trustworthiness of accounting and internal information systems.
- k) Serve as a link between the company and its shareholders.
- l) Approve the policies of information and communication with the different kinds of shareholders, the markets, interest groups and public opinion in general.
- m) Monitoring the efficiency of the implemented practices of Corporate Governance and the level of compliance with the norms of ethics and conduct adopted by the company.
- n) Proposing the policy for buying back its own shares (or treasury stock).
- o) In general, proposing operations which commit the disposal of the company's strategic assets as well as major share operations.
- p) Handle conflicts of interests between the shareholders, senior management and members of the Board of Directors, and control linked transactions.
- q) Planning for the turnover of personnel on the Board of Directors and senior management.
- r) In the absence of a policy on this matter, supervising the creation or acquisition of shares in special-purpose entities or those domiciled in countries or territories regarded as tax havens, as well as transactions or operations of a similar nature that due to their complexity, may undermine the transparency of the group.

The exercise of its functions should also be based on the principle of protecting the shareholders as a whole, particularly the minority shareholders and other legitimate interested parties. Some of the functions of the Board of Directors just described are often missing from the by-laws of companies; nevertheless, they are crucial for the effectiveness of the company.

For example, it is especially important for the Board of Directors to design and supervise a plan for replacing a retiring president of the Board of Directors and retiring CEO. This is of critical importance in cases when the president of the Board of Directors and CEO have assumed a great many responsibilities, since an adequate foresight in this respect will minimize the impact of a turn-over on the progress of the company when leadership changes.

KEY RECOMMENDATIONS	Recipients		
	Listed	Non Listed	Financial Entities
44. Non-delegable powers	✓	✓	✓

III.3. Regulation of the Board of Directors (Guideline no. 20)

As happens with the Annual General Meeting, current trends in Corporate Governance are emphasizing the need to revitalize the activities of the Boards of Directors and make them dynamic. This way the members will be required to participate in an active way as they have the necessary information to come up with sound opinions, and vote in a reasoned and justified way on aspects corresponding to the Board of Directors.

Along this line of thought, it seems evident that all companies should count on a set of **regulations for the Board of Directors** governing its organization and functioning; they should be binding on its members and imply sanctions for its violation.

As a general rule, the regulations for the Board of Directors should be approved by the board itself. On the contrary, they would lose the flexibility which represents one of the biggest advantages of these kinds of internal norms, along with the fact they are public and known, making it difficult for non-compliance.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
45. Regulations of the Board of Directors	✓	✓	✓

III.4. Size of the Board of Directors (Guideline no. 21)

In line with the aim of revitalizing the activities of the Board of Directors, the critical aspect of its size should be considered. It has been shown that boards with an excessively large number of members significantly weaken their degree of effectiveness, while extremely small Boards of Directors make difficult to create committees.

To avoid this problem, **the size of the Board of Directors should be adequate** in order to maintain the administration and governance of the company as effective as possible, and count on the participation of significant shareholders in the administrative body through the nomination of candidates for the position of Director.

In this sense, it is important to point out that no matter the circumstances, the company should avoid enlarging the number of members of the board to “accommodate” specific shareholders who, basing themselves on a certain holding in the company, hope or demand that they join the Board of Directors. In determining the number of members, the needs and efficiency of the body should be the priority. Consequently, the aspirations of specific persons or shareholders should be adjusted to that reality.

The Board of Directors will be made up of the number of members stipulated by the by-laws or within the limits they fix. It is up to the general meeting to determine the number of directors within the minimum and maximum limits established in the by-laws. We recommend that its maximum size will depend on the size of the company itself, which, in most cases, would justify a number set between seven to nine members. In the case of large listed companies, this number may be raised to eleven, since it does not seem that the real management and governance needs of the company would require a higher number.

A number of directors as the one proposed would be sufficient to form all the committees generally found in this kind of company (Auditing, Nominations & Remuneration, and Risks, etc.).

Bearing this in mind, the president (chairman) of the Board of Directors should not have a casting or superior vote. It would be recommendable that **the number of directors is odd**, to avoid possible ties in votes.

In accordance with the practice established in some countries, deputy directors are appointed with the titular directors. However, the practice of naming deputies does not usually help with the sound functioning of the Board of Directors, beyond the formal aspects associated with the regulations on quorums and attendance.

From another perspective, some companies feel the need for the quasi-participation of the deputies in the everyday dynamics of the Board of Directors, by making them attend the ordinary meetings, granting them the right to speak and even paying for their attendance. They only limit their right to vote when the titular director is present.

While it is true that this practice enables the deputies to be sufficiently informed, its direct consequence is to double the members of the Board of Directors. This implies increasing the number of directors in an inappropriate manner; and creates boards that are too large.

It would be logical to think that when the shareholders elect the persons they want on the Board of Directors they should try, as far as possible, to attract a limited number of competent candidates. With their support in the functioning of the administrative body, they will help in the process of creating value. For that reason, **we do not regard the appointment of deputy directors as necessary**.

If, for other reasons, a given company decides to maintain deputy directors, it should establish the grounds for deputies in its statutory norms and it should stipulate for each deputy director to be assigned to a specific titular director. In any case and in an unavoidable manner, it should ensure that the titular director and the deputy are always fitted into the same category of members of the Board of Directors. For example, an independent director should only have another independent director as his deputy, and the same in the rest of the cases.

KEY RECOMMENDATIONS	Recipients		
	Listed	Non Listed	Financial Entities
46. Suitable size of the Board of Directors	✓	✓	✓
47. Odd number of directors	✓	✓	✓
48. Treatment of the position of deputy directors	✓	✓	✓

III.5. Categories of the members of the Board of Directors (Guideline no. 22)

A. Categories of the Directors

With the aim of faithfully representing the shareholding structure of the company, the Board of Directors should have **different categories of members** that will represent a different view in accordance with the source of his appointment. These categories are the following:

A.1. Internal or Executive Directors: these are the ones with executive powers and senior management functions in the company or affiliates.

A.2. External Directors: represent the set of general and scattered interests that concur in a company and among the major shareholders, without being linked to the day to day management of the company.

This category is also broken down into three types:

- **Asset-holding External Directors:** these are the representatives of shareholders who are legal entities and/or physical persons. It also includes individuals proposed by them or have a personal or professional relationship with the shareholders, who are not employed by the company and whose membership on the Board of Directors derives, directly or indirectly, from their share in the patrimony (capital) of the company and the decision of a specific shareholder or group of shareholders acting in a joint manner. In several countries, these kinds of directors are also known as shareholding directors, owner-directors or non-independent directors.
- **Independent External Directors:** people with wide professional prestige who may contribute with their experience and knowledge to the administration of the company and whose link with the company, its shareholders, directors and members of the senior management is not exclusively circumscribed in their membership to the Board of Directors, which does not prevent them from holding a small amount of shares in the company.
- **External Directors:** these are the persons who cannot be named internal, executive, asset-holding or independent directors, due to their personal circumstances or of the company.

The inclusion of independent directors was originally related to the “free float” capital of large listed companies, most of which was made up of minority shareholders. In practice and given the physical impossibility of grouping “free float” capital together to nominate or elect a director; the membership of an independent external director on the Board of Directors responds, generally, to the wish of one or several shareholders. They represent a significant percentage of the company’s capital and they imply to renounce to the election of more asset-holding directors that could correspond to them, choosing instead to nominate and use their votes to elect independent directors.

As a consequence, in the case of listed companies, it is recommended that the “free-float” capital is regarded as the criterion for determining the number of independent external directors, so that the “free float” percentage corresponds as much as possible to the percentage of independent external directors on the Board of Directors.

In the case of companies not listed, even in the case of family companies with closed capital, the appointment of independent external directors usually corresponds to a governance decision by the shareholders, who understand the convenience to include people who have different points of view on the Board of Directors and are more distant from the ownership of shares.

In the region, the existence of internal or executive directors is not common especially in the case of listed companies and financial entities. As a general rule, they choose to invite the Chief Executive Officer of the company to the meetings of the Board of Directors, with the right to speak but not to vote. However, in the case of non listed companies, and particularly family companies, the use of internal or executive directors is quite frequent; it may even happen that a single person acts as a shareholder, member of the senior management, and member of the Board of Directors.

Paradoxically, as companies of this kind evolve towards a greater size or complexity, the figure of the internal director disappears, until we reach a situation where one rarely finds an internal director in the listed companies of the region or such a figure may even be poorly regarded or seen as a detrimental element.

It is worth asking why in the transition from a closed non listed company to a listed one, the directors who have helped the company to evolve and grow are no longer considered to be suitable as members of the Board of Directors of the company which has managed to evolve towards to a larger size and higher degree of professionalism.

For that reason and as long as they are a minority, the inclusion of internal directors on the Board of Directors is highly convenient. It is a practice usually accepted in more advanced countries in terms of the development of Corporate Governance. It is also recognized by the OECD itself, since it allows the Board of Directors to be more closely in touch with the day to day operations of the business. In that way it facilitates the efficient exercise of its functions as a key body for the effective governance of a company, and even though it may delegate them, the Board of Directors always retains the powers needed to influence the day to day operations of the company.

In this perspective, the inclusion of internal or executive directors, normally the CEO is a more forceful and committed way to bring the reality of the business closer to the administrative body. The difficulties that may arise, for example, from exercising control over the management and any associated potential conflict of interest, could easily be handled when the external directors are majority.

Finally, as a general rule, we believe the Board of Directors should not allow the consolidation of a majority made up of people linked by marriage or family relationships, to the third degree of consanguinity, second of affinity or first of civil ties.

B. Allowed majority of External Directors on the Board of Directors

The Board of Directors will exert its powers to propose the nomination of directors in a way that ensures the **representation of external directors by an ample majority** over the internal directors on the board.

Likewise, the Board of Directors should try to ensure that the group of directors represents a significant percentage of the company's social capital through the presence of asset-holding external directors. This does not invalidate the soundness of the practice where certain shareholders decide

to form a Board of Directors with a majority of independent external directors when they believe that it would be a better way to defend the company's social interest.

A Board of Directors with many independent directors is not necessarily more representative than one with a majority of patrimonial ones. Thus, the important thing is to establish a supportive relationship of majority support between the board and the general assembly

On that basis, corrective mechanisms can be established that allow for the presence of independent directors that are not asset-holding, internal, or executive; their role is precisely to guarantee the interests of the patrimonial majority are not confused with the interests of the company.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
49. Different categories of members	✓	✓	✓
50. Majority of external directors	✓	✓	✓

III.6. Appointment of Board members (Guideline No. 23)

The Annual General Meetings have the sovereign power to elect the directors. The meeting's right to elect is exclusive and non-delegable. We propose that companies stipulate in their internal norms a procedure for choosing the members of the Board of Directors which rules out any intervention from the internal directors.

It will be up to the Board of Directors to guarantee that this **procedure is as formal and transparent** as possible and handled with professional criteria.

The procedure governing the election of the directors by the Annual General Meeting should be organized in terms of the following phases:

A. Determining the needs of the Board of Directors

Its main objective is to inform those shareholders who have the right to nominate candidates for the Board of Directors about the ideal mixture of functional and personal profiles needed in the Board of Directors in every circumstance.

The **functional profiles** have to do with aspects such as knowledge and professional experience, while the **personal profiles** have to do with the candidates' background, reputation, prestige, availability, leadership, role in group dynamics, etc.

Whatever the kind of company, the Board of Directors itself is the most suitable body when it comes to informing the shareholders of its needs, due to its knowledge of its own dynamics and the conclusions derived from its annual evaluations.

B. Search for candidates for a director position.

Different actors, mainly controlling, significant or family shareholders, groups of shareholders, institutional investors (when they exist) and the board itself are qualified to select candidates

once the needs are identified. This process is usually spontaneous and is based on contacts, personal relations and references from third parties, although on occasions it may also rely on the advice of firms specialized in the selection of high-level personnel.

Especially, upon the reputational risks that may result hiring **former public officials** to the Board of Directors and other positions of great responsibility, and the possible lack of specific regulations on the terms of ineligibility which apply to such cases, the Board of Directors should **approve a policy for electing and hiring** such persons.

In these two initial phases, we agree with the premises of the OECD. In its *Principles of Corporate Governance* (2004) it assigns a key role in these phases of identifying needs and searching for candidates to the Board of Directors, when it states that “the board has a key role in identifying potential members for the board with the appropriate knowledge, competencies and expertise to complement the existing skills of the board and thereby improve its value-adding potential for the company”.

C. **The evaluation of the candidates** is a critical phase of the process and without a doubt the most complex one to implement, to the point where most of the possible options show weaknesses.

In this phase, the suitability of the candidate in terms of the needs of the Board of Directors must be determined through an evaluation of a set of criteria that define the profiles of the candidates and verifies a number of objective **requisites** for becoming a director and other ones for being an independent director. A positive evaluation of the criteria and the fulfillment of the requisites for being a director will determine the **suitability** of the **candidate**.

We believe that the evaluation of the candidates should be an activity undertaken before the meeting of the Annual General Meeting, so that the shareholders are provided in advance with sufficient information about the candidates proposed for the position of director. The evaluation of candidates for the director position should not exclusively depend on the will or resources of the shareholder or group of shareholders who chose the candidate and wish to nominate him/her for a position on the Board of Directors.

Furthermore, we believe that an evaluation of the curriculum vitae of the candidates alone is an insufficient mean for determining the suitability of a given candidate to become a director. A priori, regardless of the kind of company, we believe the only body in the company with sufficient resources to evaluate the suitability of the candidates is the Board of Directors of the company itself.

In the case of companies with specialized Nominations and Remunerations Committees, it is assumed that this evaluation will be more professional. There is also no doubt that this process of evaluating the candidates for a director position may be undertaken in an even more independent way if the company uses external resources, such as the opinion of a firm specialized in the selection of personnel (a “headhunter” firm).

Different countries are starting to use this type of assistance especially for evaluating candidates for an independent external director position. Evidently, the role of the Board of Directors in evaluating the suitability of candidates for a director position would be undertaken in a much more efficient way if the directors were **chosen or replaced in a scaled manner**. Thus, the administrative body would permanently be engaged in that process and create a situation where “*some directors with experience on the Board of Directors are always awaiting for the new ones*”, and so on and so forth.

Nevertheless, the combination of options for proposing candidates for a director, and the different voting mechanisms (electoral quota, cumulative voting, simple majority, nominations by the minority, closed lists, individual election, co-optation, etc.) currently in force in every national legislation for their election may have a direct and substantial influence on both the final qualitative composition of Boards of Directors and the body or organization competent to evaluate the suitability of the candidates proposed for a director.

D. Nomination of candidates at the General Meeting

With the aim of minimizing the risks of a possibly mistaken implementation, this text would grant the outgoing Board of Directors the power to nominate candidates for a director position before the Annual General Meeting. It is the best method, in terms of pragmatism and simplicity, to ensure due compliance with the essential standards of Corporate Governance just mentioned, and consequently guarantee a full and effective implementation.

In no way this proposal intends to suppress the inviolable right of the shareholders to directly propose their candidates for a director to the Annual General Meeting, if they wish to.

However, complying with that right we believe that with sufficient notice in advance and before the holding of the Annual General Meeting, the Board of Directors is the most suitable body for centralizing and coordinating the process of forming the administrative body. The shareholders, who based on their share percentage, wish to join the board, should set forth their aspirations, negotiate the balance between the wishes of the shareholders and distribution of the different categories of directors, be familiar with the needs of the Board of Directors, present their candidates for a director and accept that these candidates will be evaluated.

Under this approach, any shareholder who insists on nominating directly his candidates for director before the Annual General Meeting would be acting in a legitimate way. In practice, he/she would be acting as an “outsider” with regard to the other shareholders who have agreed to undertake a coordinated and transparent process in which the evaluation of the candidates is a key matter.

E. Election of the directors

The election of the directors is the final phase in the process of forming the Board of Directors. It takes place during the meeting of the Annual General Meeting. There are different

mechanisms or voting systems for the election of the directors and some countries in the region have laws about the obligatory use of one or another system. Others, by contrast, leave it up to the company to apply the system it believes is most convenient.

Regardless on the kind of company, there is no doubt that the best option is to arrive at the Annual General Meeting with a slate or a single and closed list of candidates for the director position. The candidate should have won the consensus of an important group of shareholders who represent a very large percentage of the company's capital. The degree of acceptance, measured by the percentage of favorable votes given to the list, is the barometer that indicates the sensitivity and correctness of the negotiations to form a Board of Directors through a single list.

For example, in the case of a listed company with an ample capital float where the single list includes directors labeled as independent ones, objectively, the list will receive an even larger support from the minority shareholders if those shareholders assume that the directors labeled as independent are in fact independent in practice.

Of all of the voting mechanisms for the election of directors, and regardless of the kind of company, we propose the **cumulative vote** as long as it is legally permissible. We believe it is the fairest as it includes directors with different approaches. This avoids situations where the controlling shareholder, when he/she exists, votes alone to determine the composition of the entire Board of Directors.

Assuming the electors have to choose among alternative candidates, the legal framework should determine the possibility to introduce the mechanism of the cumulative vote as the most suitable one to be adopted by companies when electing directors. It is the only mechanism that guarantees shareholders with significant participation will be able to nominate specific candidates for the Board of Directors. The only exception would be in cases when there is a single list of candidates previously agreed upon through a consensus among the shareholders.

From a strictly legal point of view, it is the only instance where the principle of one share, one vote does not apply, since under the mechanism of the cumulative vote, each share has as many votes as there are directors to be elected. Nevertheless, that system is widely employed and accepted in several countries where the principle is in force, as it offers advantages over the other existing voting mechanisms.

The proposal and appointment of members of the Board of Directors should be subject to a formal and transparent procedure, with a **proposal justified by the Nominations and Remuneration Committee** if it exists, or, by the Board of Directors itself in the contrary case. We infer that the action of the Board of Directors can and should play a key role in forming the administrative body, whether directly or through the Nominations and Remuneration Committee when it exists.

This model, known as the “board-driven” model, does not aim at or is allowed to suppress the inviolable right of shareholders to elect the members of the Board of Directors at their assembly, opposed to what is known as the “shareholders-driven” kind. In this model, the Board of Directors itself executes a number of prior tasks for which it counts on some resources and that the shareholders lack.

Notwithstanding this advantage, it is necessary to reach certain equilibrium between the two models through a dynamic Assembly where the shareholders fully exercise their rights. If this counterweight does not exist, the “board-driven” model may induce the directors to remain on the board for an indefinite period.

The company should stipulate the necessary requisites a candidate should have to be eligible for the director position, through by-laws of a general nature and more specific regulations on the qualifications a director must have.

Among the **most important requisites for becoming a director**, the following stand out:

- Qualification and professional prestige, experience and proven trustworthiness.
- The middle-age requisite for the Board of Directors is a range between fifty-five and sixty-five, with a minimum limit of more than thirty-five.
- The director should not have positions or undertake functions of representation, supervision or consultancy for competing companies or have the same positions or functions in companies with a dominant or controlling position in competing companies.
- A director should not simultaneously be a member of more than five Boards of Directors, excluding, the boards of different affiliated companies or administrative bodies of those companies when the director’s patrimonial, personal or family position grants him the right to be part of it and of philanthropic institutions.
- Persons who, in themselves or in representation of others, have positions in companies that are clients or habitual suppliers of goods and services to the company, either as representatives of those entities or through links with them, may not serve as members of the Board of Directors. This situation may cause a conflict or clash of interests between the candidate and the company. An exception is made for financial entities serving as suppliers of financial services to the company.
- Anyone who is subject to judicial proceedings, directly or indirectly, and may eventually jeopardize the reputation of the company, may not serve on the Board of Directors.

In practical terms, the directors’ professional experience should not necessarily coincide or be based on the same economic activity that constitutes the company’s social purpose; always provided that the director has other kinds of experience and training suitable for holding his position. Nevertheless, it is up to the Nominations and Remuneration Committee to evaluate the suitability of each candidate in terms of his experience and skills, or the Board of Directors itself when no such committee exists.

In terms of age, when the Nominations and Remuneration Committee, or the Board of Directors in its absence, proposes a candidate, it should also ensure that there are no limitations of age or health which invalidate its proposal for the nomination of the candidate. The average age of the members of the board as a whole should be taken into account for this exercise.

It is convenient to clarify that the limit on the age of the members of the Board of Directors has been and still is a highly controversial matter. Not setting the maximum age for membership to the Board of Directors may go against one of the objectives good governance pursues: make the work of the Board of Directors more dynamic.

However, not setting a maximum age limit for membership to the Board of Directors allows the board to have members whose experience and knowledge, of the sector and the company itself, amount to a major asset. On the other hand, such a limit on age allows for a smoother renewal of the directors preventing unnecessary stresses in many cases. Despite reasons supporting and justifying one side of the argument and the other, we believe companies should adopt certain rules that allow directors to be replaced for reasons of age.

While it is true that the seniority of directors is a clear advantage for the company and grants the added value of experience to their opinions, the rules limiting the age of directors do not have to be so categorical to the point they force the company to miss out on the sound judgment of directors simply because they have reached a certain age. They should, nevertheless, be drafted in a way that gives the company a margin of flexibility, on a case by case basis.

We recommend the adoption of rules that limit the overall ages of the members of the Board of Directors, instead of an age limit on an individual member. **The limitation, thus, should be based on the average age of the Board of Directors as a whole.** This way, candidates of any age will be allowed to be members of the board, as they are not younger than thirty-five and have the requisite of intellectual and physical capacities. With the aim of ensuring a timely turn-over of the members of the Board of Directors, we recommend that the average age of the directors should be between fifty-five and sixty-five.

A measure to that effect enables the company to combine the experience and knowledge of the older directors while, in a way, establishing an automatic dismissal mechanism. This minimizes the tensions that could arise if there were no age limit. A measure of this kind significantly lessens the possibility that directors neglect in the exercise of their functions due to the age limit because they are aware of the possibility of an upcoming forcible retirement from their mandate.

In synthesis, replacing older members with younger ones in the board, allows for more dynamism. The same applies when that dynamism is harmonized with the seniority and sound judgment of the older members. In addition to the requisites and criteria mentioned, when **family relations** or other ties exist among some members of the board that could affect or jeopardize their independence of judgment, **the assembly should be informed** so it can assess that circumstance.

Finally, if the proposed candidate is a member of other Boards of Directors, the Nominations and Remuneration Committee or the Board of Directors in its absence, should judge whether the number of boards where the candidate is a member, and his dedication to those functions, could disqualify him from the nomination.

The responsible parties should also determine if there are possible situations of conflict of interest, as occurs when the candidate is part of boards of rival companies, clients or suppliers of the company.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
51 Specific procedure for selecting and proposing members	✓	✓	✓
52 Justification of the proposal by the Nominations and Remuneration Committee	✓	✓	
53 Majority of External Directors on the Board of Directors	✓	✓	✓
54 Renewal of board in a scaled manner	✓		✓
55 Cumulative vote	✓	✓	✓
56 Justification of the proposal by the Nominations and Remuneration Committee	✓		✓
57 Requisites to be a director	✓	✓	✓
58 Limit on the average age of the members of the board	✓	✓	✓
59 Information on the family relationships of the directors given to the assembly	✓	✓	✓

III.7. Independent External Directors (Guideline No. 24)

A. Appointment of External Director

Given the multiple institutional and personal relations that exist among the companies of the countries in the region, it must be clarified that establishing a rule to name external independent directors, or even the idea of an independent member of the board itself, will not ensure its applicability and effectiveness. The system of electing independent members of the board has still not been perfected and we believe this situation is not exclusive to the countries of the region.

In many cases, the trend leads to appoint members with familiar or friendship relationships as their appointment derives from direct proposals by shareholders with a controlling share, the president (chairman) of the Board of Directors or patrimonial directors. This definitely implies a substantial distancing from the original idea of appointing an independent member and the very existence of independent members. It is, thus, an undeniable reality that many directors who are appointed in the guise of independent ones owe their membership to opportunistic motives, and their “independence” is only cosmetic. Those individuals with recognized professional prestige can contribute their experience and knowledge to the Board of Directors; as they are neither executive nor patrimonial

directors they ensure their impartiality and objective criteria. This makes these individuals suitable candidates as independent directors.

The mission of the independent director is to watch over the general interests of the company, given the struggle among the diverse interests, including those of the minority shareholders, at play. Given the patrimonial directors do not represent the majority nor the independent directors the minority, the external independent directors should ensure the company is administered in a way that takes the interests of the minority shareholders into account, and makes sure that the interests of the patrimonial directors are not mistaken for those of the company.

Undesirable situations where the rights of minority shareholders are violated do occur in the running of companies. However, we consider this does not justify, distrusting asset-holding and executive directors without justification a priori. The company should avoid giving the independent directors functions where they could act as a counterweight as it could gravely harm the cohesion of the board's actions.

As explained graphically, the independent director is the one who has the power to say "no" to a proposal of the president (chairman) in the Board of Directors and/or the group of patrimonial directors: the stronger this power, the greater the degree of independence will be. This will avoid situations where feeling a fear of disagreement predominates over the wish for transparency on the boards. This does not prevent the administrators from being aware of the responsibilities they assume when they occupy their position and carry out their functions, where non-compliance becomes a matter of penal responsibility in the most advanced legislations

In this sense, it is necessary to have a broad field of professional activity to be truly independent. In the economic aspect, it is also pertinent not to depend exclusively on belonging to a given Board of Directors, since a **true economic independence** substantially strengthens a director's independence of criteria.

The by-laws should establish the criteria taken into account when defining the nature of independent directors.

In our opinion, the following **requisites or conditions for being regarded as independent are pertinent**

- The candidate should not be a director or employee of a company or group that has shares in the company, independently if the company has appointed or not asset-holding directors, considering the candidate's condition as a shareholder.
- The candidate should not be the employee of a physical person who is a shareholder of the company, whether that person is a member or not of the board of the directors, or the director or employee of linked companies.
- During the previous three years, the candidate should not have had a commercial, business or contractual relation, direct or indirect and of a significant nature, with the company or any other company of the same group, its executives, patrimonial directors or any other company of the same group who has shareholding interests in the company, either in his/her own name or as a

shareholder, director or senior executive of an entity that maintains or has maintained that relation.

- Business relations will be defined as those of a supplier of goods or services, including payment for financial services, and as an advisor or consultant.
- Business relations are considered to be significant when there has been an exchange of invoices or payments for a value higher than 1% of the annual incomes of any of the parties.
- The candidate should not have a relationship of close kinship with significant shareholders, patrimonial directors, executive directors or the senior management of the company. By close kinship we refer to a spouse or a person with similar intimacy; the ancestors, offspring and siblings of the administrator or of the spouse of the administrator; and the spouses of the ancestors, offspring and siblings of the administrator.
- Those who are directors or senior executives of a different company where some director or member of the senior management is an external director should not be nominated or appointed as independent directors.
- Those who in the previous five years have been members of the senior management, or employees in the company or companies of the same group, or companies that are shareholders should not be nominated or appointed as independent directors.
- Those who receive any quantity or benefit other than the salary of a director of the company or any other company in the same group should not be nominated or appointed as independent directors, except when it is insignificant.
- For the effects of these stipulations, the complementary payments of pensions the director receives by virtue of his/her previous professional or working relation should not be taken into account, always provided that such complements have an unconditional nature. In consequence, the company responsible for them cannot suspend, modify or revoke such payments in a discretionary manner without falling into a non-compliance of its obligations.
- Those that are, or during the previous three years have been, a partner or employee of the external auditor or of the auditor of any company in the same corporate group during that period cannot be nominated or appointed as external directors.
- Shareholders, directors or senior executives of an entity or institution that receives important donations from the company or any other company in its group, or have received them during the past three years, cannot be nominated or appointed as independent directors. Those who are merely patrons of a foundation that receives donations are excluded from this stipulation.
- Those who have not been evaluated and proposed by the Nominations and Remunerations Committee, or in its absence, the Board of Directors, to appoint or renew their appointment, cannot be nominated or appointed as independent directors.
- The person should have a professional and personal profile that inspires trust in the shareholders in his/her independence.

In cases where one of these relations exist, a candidate who is proposed or a director who already sits on the board should not be regarded as an independent but simply as an external director. In the

case of acting directors, it does not exclude the need for the Board of Directors to gain knowledge of and evaluate infringements of his independence, through a prior report to the Nominations and Remunerations Committee when it exists, which should be published in the company's public annual report. The General Meeting shall be informed of this circumstance when the agreement to appoint the director is adopted.

On the contrary, other than approving the definition of independence, the task of determining the independence of a director or candidate for a director is ultimately the responsibility of the Nominations and Remunerations Committee or in its absence, the Board of Directors itself. The board may decide that while the candidate for director can fulfill the requisites for an independent director established in the country's legislation, to the candidate could not be due to the specific circumstances of the person or company.

We believe that an independent director may be reappointed, without ignoring the need for the Nominations and Remuneration Committee, or the Board of Directors in its absence, to evaluate with special care how long the director should remain on the board and whether he/she has an independent status at the moment of his reappointment.

In terms of the appointment, it is not recommendable that the independent director is elected separately by the minority shareholders; he is not a representative of the minorities in the strict sense, which does not mean that the administration should create obstacles or barriers to the possibilities of the grouping together of the minority shareholders.

As we stated above, from the Corporate Governance perspective, the great advance in this field will be seen when the controlling and significant shareholders are committed to the inclusion of truly independent directors on the Board of Directors when they deem it convenient.

B. Declaration of Directors' Independence

The selection process should be complemented with a twofold obligation that should be included in the law that applies to listed companies:

- The candidate should publicly declare as an active obligation his feeling and objectivity as independent, both to the company itself, as to its shareholders and directors, with a specific duty to indicate any factor or deed that may lead to question the independence by a third party.
- The Board of Directors itself should declare that it considers the candidate to be independent, on the basis of his own declaration and the additional queries the board may have made.

KEY RECOMMENDATIONS	Recipients		
	Listed	Non Listed	Financial Entities
60. Economic Independence of the directors	✓	✓	✓
61. Conditions needed to be considered as independent	✓	✓	✓
62. Declaration of independence	✓	✓	✓

III.8. Termination of the Appointment of the Directors (Guideline no. 25)

The by-laws should fixate the **causes for the termination of directors** as “*numerus clausus*” in a way it ensures that the same directors, in particular the asset-holding and independent ones, remain in their positions during the period for which they have been elected. The Board of Directors may not propose a termination to the assembly without citing some of the causes stipulated in the by-laws and through a **prior report recommending the termination** from the Nominations and Remuneration Committee, or in its absence, from the Board of Directors itself. Nevertheless, when a director fails to meet the conditions for his appointment, especially in cases when the prestige or good name of the company could be damaged, the director should immediately resign.

We believe that the termination proposal to the Annual General Meeting is justified in the following cases:

- If the director is internal or executive, as soon as resigning from the position associated with their appointment as a director.
- When the director violates one of the legal rules on incompatibility or prohibition of membership of the board.
- When the conditions of the permanence on the Board of Directors may negatively affect its functioning, as a consequence of a negative annual evaluation, or when the trustworthiness or reputation of the company in the market is jeopardized or place the company’s interests at risk.
- In the case of a patrimonial director, when the shareholder whose shareholding interests he/she represents on the board rids himself of his share in the company.
- When, in the course of a financial year, the director fails to attend a significant number of meetings of the board without a justified cause. The definition of “significant” will be determined on a case by case basis, in terms of the number of meetings the Board of Directors programs each year. Nevertheless, as a general guideline, we suggest the following percentage of absences to meetings called per year: three absences out of twelve meetings; and two absences out of six meetings.

Likewise, in any circumstance, the Board of Directors may take the initiative of asking a director to resign, if it believes that a director has violated any of the requisites previously mentioned.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
63. Causes for the termination of directors	✓	✓	✓
64. Prior report supporting termination	✓	✓	✓

III.9. Regulation of the rights and duties of the members of the Board of Directors or Administrators (Guideline no. 26)

A. Duties of the Directors

The regulation of the diligence and loyalty of the members of the Board of Directors or administrators is a crucial aspect of Corporate Governance. Particularly in view of the unfortunate experiences that have recently occurred, there is no doubt that good Corporate Governance requires defending the company from the possible incompetence or negligence of its directors. Also above all it prevents directors and managers from executing acts of unwarranted appropriation of the goods of the company who in many cases have put their personal interests above those of the interests of the company. Currently, the commercial legislation of the countries of the region on the responsibility of administrators shows severe deficiencies, and even worse, has been consolidating a certain feeling of impunity. In reality, there are no effective means to demand that the directors face up to their responsibilities. Furthermore, except for certain exceptions, the duties of administrators have not been sufficiently clarified by the law. It only includes generalities without being specific at all, which implies that infractions of those duties are not defined.

Upon the difficulty of relying on self-regulation to enforce all of the rules and measures regarding the definition of the duties of administrators, the legislator should establish a detailed legal framework for the contents of the duties of directors. This way there would be a stronger link between the norms on the same and the requirement that the administrators of companies are responsible for honoring them.

It is evident that there are many ways that a director may obtain unjustified advantages. For example, the simple fact that a control premium that is completely out of proportion compared to its real value is offered and paid by a company. This is striking proof that the payments and fees paid to the controlling shareholder and directors do not always respect the principle of equal treatment. This practice of overvaluing the control premium is a characteristic of less developed markets where norms of good Corporate Governance are not adequately implemented and there is a meager development of legislation applicable to the stock market.

The **duties** that in our opinion should be included in the **by-laws** of companies adopting the Guidelines are specified as follows (it does not exclude the convenience of turning all of these aspects into legal norms in the countries of the region):

- A.1. **The duty of due diligence:** the director should comply with the duties imposed by the laws, the by-laws of the company and the other internal norms that guarantee fidelity to its social interest, understood as the company's interest in creating value in benefit of the shareholders.
- A.2. **Duty of loyalty:** the directors should act in good faith, in the interest of the company, with the honesty and conscientiousness of someone who manages another's business.

The director should not exploit the name of the company or the position to undertake operations on his/her own account or that of linked persons, nor use his powers for ends other than those for which he has been appointed.

No director may undertake investments or transactions related to the goods of the company: neither for his/her own benefit or that of persons linked to him/her; nor those he/she gained knowledge of when exercising his/her position, when the investment or transaction was offered to the company, or he had some interest in it. Always provided that the company has not expressly ruled out that investment or transaction without taking into account the influence of the interested director.

The director may not charge commissions for signing contracts between the company and its suppliers, nor for the provision of the company's services to third parties.

A.3. Duty of non-competition: this duty implies a double obligation of information and impossibility of providing services to the competition for a given period after the resignation.

- The directors should inform about any shareholding or business participation they have in the competition companies, as well as the positions and functions they exercise in those companies. They should also inform the execution, on their own account or of another, of activities similar to those of the company's social purpose.
- The by-laws may stipulate that the director leaving the company may not accept an appointment as a director of a competing company for a period of two years, counted from the time of his resignation, except when the Board of Directors of the company expressly authorizes it without prejudice to the enforcement of the applicable norms.

Experience shows that clear rules should be established to prevent the resigning director, who is also an executive, from entering into a competition process with the company left. The resigning director could attract the most qualified personnel, the clients or use information about the company left for the benefit of the new employer. It does not seem that the limitations on providing services for the competition should be extended to the independent or asset-holding directors. In any case they would remain bound by the obligation of secrecy explained in the following paragraph.

A.4. Duty of secrecy: the by-laws should establish the rules of secrecy applicable to the directors, which, as a minimum, should include the following:

- Directors, both when exercising their office and after resigning, should guard the secrecy of the confidential information and data of the company, or associated matters they learned when holding their position.
- Except when the law allows for it, such information cannot be published or divulged.
- The director may not use non-public information of the company for private ends, unless a prior agreement has been made with the Board of Directors.

A.5. Duty not to use the company's social assets: the director may not make personal use

of the assets of the company, nor use the power attained to the position to obtain a patrimonial advantage that does not correspond to his functions, unless appropriate compensation was made.

B. Rights of the Directors

If duties are assigned to the directors, the correct exercise of their position also requires they count on a set of rights. This way the work of the directors is formally strengthened. The right to information is the keystone on which the diligent exercise of the position of director rests.

B.1. The right to information: The director may demand to obtain the information associated with the aspects he/she is responsible for and all the information regarded as relevant for the correct exercise of the function of his position. This allows the director for the adequate performance of his/her functions. No exceptions should be admitted at any time under the pretext of confidentiality.

Specifically and as a minimum requirement, the by-laws should stipulate the right of directors to:

- Obtain information about any aspect of the company, examine its books, records and documents, contact those responsible for running different departments and visit the company's installations. Always provided that the performance of the functions requires it, except in cases of especially confidential information, in which case will be determined by the management of the company.
- Obtain and dispense information about the matters to be discussed at the Board of Directors meetings, with sufficient notice in advance and in a due form that allows for its revision. The only exception is for matters requiring a special confidentiality that will only be divulged in the course of the Board of Directors' meetings.

B.2. The right to count on the help of experts: The by-laws should allow directors with the possibility to obtain help of external or internal experts of the company. The directors should be able to obtain the help of the internal experts of the company when carrying out their functions. They should also be able to request the Board of Directors to hire external consultants to help with possible problems that may arise when exercising their position, in cases when there are specific problems of a certain prominence and complexity.

The by-laws should establish exceptions when exercising this right if the Board of Directors considers that the right is unnecessary, its cost is out of proportion to the importance of the problem and the assets and income of the company, or if that consultancy may be adequately provided by experts and technicians from the company itself.

B.3. Right to remuneration: the directors should be sufficiently paid for exercising their position. Given the complexity of the field of remuneration, a specific guideline for this matter is presented in this document.

B.4. Right to training: when the directors join the Board of Directors for the first time, they should have the right to receive an adequate induction to the reality of the company, its complexities and key facets. This will allow them to attain a profound view of the company in the shortest possible time possible.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
65. Definition and regulation of the duties of the directors in the by-laws.	✓	✓	✓
66. Definition and regulation of the rights of the directors in the by-laws.	✓	✓	✓

III.10. Conflicts of Interest and Related-party Transactions (Guideline no. 27)

A. Conflicts of personal interest

The treatment of conflicts of interest is a very controversial subject, and even more when referring to the members of the Board of Directors and senior management. As a general principle, in the face of a conflict of interest between the company and a member of the Board of Directors or the senior management, the duty of loyalty is what should guide the decision and, consequently, social interest should always be the priority. It is not possible to avoid conflict of interests in an absolute sense. In fact, potential conflicts of interest are practically inherent to the functioning of any company.

There is a strong possibility that in the course of handling the affairs of the company situations may arise producing a conflict of interest between the company and a director or member of the senior management. In terms of Corporate Governance, the objective is that **the internal norms of the company establish a definite and formalized procedure for administering and managing conflicts of personal interest.** Thus, the procedure provided must determine the nature of the conflicts of interest; that is, if the situation of conflict of interest is sporadic, or of a permanent nature.

If the conflict of interest is sporadic, the internal norms of the company should provide a mechanism indicating the applicable procedure, giving detailed rules and steps to follow. This should be relatively easy to administer and difficult to evade. In the case of a permanent conflicts of interest, the procedure should consider that situation as a reason for obligatory dismissal or, in its absence and if possible, a termination proposal.

In every case, the persons affected by a conflict of interest should inform the Nominations and Remuneration Committee, or the Board of Directors, of any situation of conflict of interest, direct or indirect through related parties that might involve the general interest of the company. In statutory terms, in cases where there is a conflict of interest affecting a director, the rules should stipulate that that the director should abstain from voting at the moment of evaluating that situation.

The relevant situations of conflict of interest that involve the directors should be made public on an annual basis. For the effects of the provisions in this section, it is recommendable that the by-laws specify the conditions leading someone to be regarded as linked and, thus, establish an obligation to inform the company of that status.

In line with the International Accounting Norm no. 24 (IFRS, 24), the following are regarded as having links with the directors:

- The spouse of the director or the person with whom the director enjoys a similar relation of intimacy.
- The forefathers, offspring or siblings of the director or the director's spouse.
- The spouses of the forefathers, offspring and siblings of the director.
- The legal entities in which the director, or any of the persons mentioned above with whom the director is linked, has a significant and stable share of capital or the capacity to intervene in decisions about the financial policy and exploitation of the entity. While not having control of the same, the person may obtain the capacity of intervention by holding shares in the company, through legal or statutory stipulations or agreements.

It is especially important the necessary personal extension of duties and the involvement of linked persons in situations where the director is a legal person.

Moreover, the extension of duties to the director who is a legal person should be defined more clearly in these cases, since the cause of his behavior is more opaque than in the case of administrators who are physical persons. Consequently, the following should be considered as linked persons:

- De facto directors, including shadow directors or directors by right.
- Liquidators.
- Representatives with the general powers of the director who is a legal person.
- Companies in the same group.
- The persons that have the status of people linked with the directors in accordance with what was stated above, with respect to the representative of the director who is a legal person.
- Annually, the directors and members of the senior management should present and permanently update a general statement of their links (a map of linked parties).

B. Conflicts of Interest due to Activities

As for financial entities, by the very nature of their activities and as a consequence of the possible complexity of their structures, their volume of transactions and the diversity of the financial services they provide, situations of conflict of interest may arise. They may affect the entity itself, the relation between the entity and its clients, and the relation among the clients themselves. As an example, conflicts of interest within a financial entity may take the form of a variety of situations, such as:

- Provide clients with advice on investments or manage their portfolios at their own discretion, and simultaneously establish an investment fund or negotiate securities on its own account (trading account).
- Receive mandates from clients of an investment bank incompatible with the entity's strategies or with mandates received from other clients.

Furthermore, the following situations of conflict of interest may arise in the relations with clients, among others:

- The entity or the responsible executive may obtain a financial benefit or avoid a financial loss at the expense of the client.
- The entity or the responsible executive has a personal interest in the result of a service provided to the client or a transaction on the client's behalf which is different from the client's interest in that result.
- The entity or the responsible executive has financial incentives or incentives of another kind to favor the interests of another client or clients over the interests of its client.
- The entity or the responsible executive is engaged in the same activity as the client.
- The entity or the responsible executive receives or is going to receive an incentive from a person other than the client for a service provided to the client, in the form of money, goods or services, in addition to the normal commission or fee for that service.

As a consequence of this, **the Board of Directors should approve a Policy on Conflicts of Interest due to Activities** to identify the circumstances that could potentially cause conflicts of interests. The Policy should also specify the procedures to be followed and the measures to be adopted to prevent and handle such conflicts, in order to avoid or end the conflict of interest, or in the last resort, reveal it to the client.

C. Transactions with related parties

It is a frequent reality that conflicts of interest are also associated with a related-party transaction or operation, where the good object of the transaction may be shares in the company or other types of goods or services, such as financial operations, supplies, leasing, warranties, the purchase and sale of assets, etc.

These types of transactions between the company and members of the Board of Directors, controlling or significant shareholders, members of the senior management, or parties linked to any of them, or between companies in the same corporate group ("intra-group" operations), are one of the clearest expressions of the vices and the virtues of a company.

Related-party transactions arise more frequently in situations where a single shareholder has a controlling interest and in corporate groups ("intra-group" operations). These circumstances present a special problem in managing the transactions, especially when the parent company does not control 100% of the capital of the subsidiary one. When this situation occurs in countries whose legal framework focuses on individual companies, it may place the directors of the subsidiaries in a

problematic situation if they put the general interest of the group before the particular interest of the subsidiary when the linked transactions are evaluated.

Therefore, related-party transactions are not necessarily negative per se. They may even bring economic benefits and create value, but it should not be concealed that in occasions they may entail a risk of abuse or unwarranted appropriation (“tunneling”), to the detriment of the minority shareholders and to the benefit of the persons closest to the administrative bodies of the company.

The treatment of related-party transactions is even being dealt with in a good number of countries on a regulatory level, to the point where there is an IFRS norm (specifically, NIC 24) that defines a *related party* of a company and specific norms on financial information which apply to financial information on linked transactions that allows for their clear identification and analysis. As happens with situations of conflict of interest, the key aspect of linked transactions for any kind of company is that it has a formal policy that defines the **procedure for their evaluation, eventual approval and disclosure**.

As a general principle, a policy for the suitable treatment of these types of operations must cover the following aspects, whose scope will depend on the kind of company, since the requisites must be stricter for listed companies and financial entities:

C.1. Evaluation: Gaining knowledge and evaluating the transaction should be the responsibility of the Auditing Committee, with a strong presence of independent directors, or in their absence, the Board of Directors itself, in which case it would be desirable that the weight of the evaluation fall on the independent directors.

The conclusions of the evaluation must be published in a report sent to the Board of Directors where the following is determined:

- The qualitative or quantitative criteria used to determine the feasibility of the transaction.
- Respect for equal treatment of all of the shareholders of the operation.
- The price or value of the operation and its relation to market conditions.
- The time of the disclosure.

The intervention of independent consultants may be considered for the evaluation of especially important or complex related-party transactions. The same applies to direct or indirect transactions that can be undertaken between companies belonging to the same corporate group (“intra-group” operations).

C.2. Approval: related-party transactions must be approved by the Board of Directors, excluding the interested party, and depending on the volume and complexity of the operation, the company’s policy may establish the option of requesting the approval of the Annual General Meeting.

In addition to the report just mentioned, a qualified majority of the Board of Directors may be required for the approval of the more important transactions that we believe could be composed of at least three quarters of the board and/or the affirmative votes of the independent directors. Nevertheless, when recurrent related-party transactions

are undertaken, the express authorization of the Board of Directors is not required. This occurs specifically in transactions made by virtue of a contract of adhesion or general framework agreement, whose conditions are wholly standardized and applied in a massive form when carried out at market prices fixed in general by the person acting as supplier of the good or service and when the amount is not relevant for the company.

C.3. Disclosure: it is desirable that the ex post divulgation of the related-party transactions, normally completed through periodical reports, follows the scheme proposed by the IFRS, as in the case of recurrent transactions at market prices.

For their part, non-recurrent material transactions should be reported within a short period of time following their approval, which should not surpass seven days.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
67. Procedure for managing conflicts of personal interest	✓	✓	✓
68. Policy for conflicts of interest due to activities			✓
69. Map of related parties	✓	✓	✓
70. Policies for evaluating, approving and disclosing related-party transactions	✓	✓	✓

III.1.1. Director's Compensation (Guideline no. 28)

One of the most controversial aspects of Corporate Governance is the remuneration of the members of the Board of Directors; it has become especially polemical following the world economic crisis that began in 2007-2008. The current trend is that companies should adhere to the framework of transparent information and disclose the remuneration of their directors and senior managers. As a general principle, the remuneration of the directors should have the following two characteristics:

- It should be public and transparent, so that shareholders and interested third parties are aware of it.
- It should be sufficient to prevent conflicts of interest and lack of independence, and also linked to a certain extent to the results of the company.

It can be affirmed that for an effective functioning of a company, **the Board of Directors should be sufficiently compensated** and that this payment be of public knowledge. In several countries of the region a low, if not testimonial, compensation is currently being promoted.

We believe this position does not lead anywhere, since it limits the possibility of requiring the director to fulfill his/her commitments and it may lead to unjustified and uncontrolled payments. These payments are the cause of many problems that widen the gap between the interests and motivations of the minority shareholder (a dividend and value creation) and the more significant sharehold-

ers. Given the possibility of major shareholders to participate in the administration and management of the company, receiving a large payment becomes a further motivation, along with the benefits derived from participation in linked transactions in the worst cases.

In addition, a low remuneration is justified in many occasions because of the existence of intangible benefits from belonging to a Board of Directors, such as public respect and a favorable image. While it is true that an intangible component may in fact exist, in no case should it replace a tangible or economic remuneration. In the end, economic remuneration represents the shareholders' acknowledgment of the value added to the company by the members of the board.

There are currently different alternatives to regulate the remuneration of members of the Board of Directors that basically have to do with the variable component. In a certain way, the idea is to link the salaries of the Board of Directors and the senior management to the long-term progress of the company and avoid some of the following situations:

- Excessively high payments, derived from excessive variable components.
- Excessively low payments that does not motivate the members of the Board of Directors and discourages the attraction of profiles suitable to integrate the board. One should not forget the rule that states that "the type of director you'll have will depend on what you pay".
- Payment structures not governed by criteria that take into account the true contribution of the members of the Board of Directors.

Thus, it might be affirmed that the shareholders expect that the payments to the Board of Directors do not exceed what is needed to link competent people to the company. In one way or another, these payments will be consistent with the performance of the director, based on the results of the annual evaluation of the director and the company.

This aspiration necessarily rests on the need to have certain levels of information that allow the shareholders to scrutinize or evaluate the soundness of the remunerations the directors are to receive.

A. Compensation Policy

All matters related to the compensation of the Board of Directors and the senior management have attracted significant attention in several countries in the world. This is due to the serious problems that have become evident since the beginning of the world crisis in 2008. At that time, the existence of unsuitable remuneration schemes especially in financial entities led to excessive risk-taking which, in the middle term, has meant a substantial loss of value for shareholders if not the utter destruction of value.

The establishment of a **retribution policy** for directors should include, in the first place, all of the components of a satisfactory remuneration of the directors, such as the size of their fees, allowances and any other payments arising from the exercise of their position. Regardless of its cause, in the form of money or any other kind, it should also include the company's obligations in the form of

pensions or life insurance policies, both for former and current directors, as well as civil responsibility insurance policies paid by the company in favor of the directors.

In general, we believe the General Meeting is the social body with the power to approve the guidelines of the policy for paying the Board of Directors, always provided there is a reasonable proposal from the board, backed by a prior report from the Nominations and Remuneration Committee, or, in the opposite case, from the Board of Directors itself.

In addition to what was previously mentioned, the key aspects of a policy of remuneration for the Board of Directors should be, in general, the following:

- A.1.** The compensation to the Board of Directors should be designed on the basis of fixed and variable components, so that it will be compatible with the aims of the company, the degree to which it assumes risks, and the risks which are thus assumed.
- A.2.** In the total annual remuneration, the fixed and variable components should be duly balanced. The fixed component will be an important part of the total one, so that the variable component may be designed in a flexible manner.
- A.3.** The total retribution should take into account the performance of the directors, and thus, consider their membership on committees. It should also evaluate the work of the president (chairman) of the Board of Directors or the created committees, so that payment is aligned with the level of actual responsibility and real dedication of each director, following the principle that “pay more who works more”.
- A.4.** The fixed component will derive from the mere fact of being a director; and normally will be in the form of an allowance for attending the meetings of the board and eventually, a fixed monthly fee. In addition, the fixed component should take into account the level of responsibilities of the functions carried out and should be reasonably equivalent to that of similar companies so that it enables to company to attract and retain talented people on the Board of Directors.
- A.5.** Within the framework of the limit set by the policy for remunerating the directors, the fixed component should:
 - Avoid being so significant that it leads to the strong assumption or risk taking, especially in the short term.
 - Be linked to the performance of the company, its long term objectives and profitability to the shareholders, taking into account the level of risks assumed; that is, it should be aligned with the interests of the shareholders.
 - When share options or payments linked with shares are included in the variable component, their actual payment should be in the long-term, even when the directors leave the board, always provided they do not withdraw because of a serious non-compliance with their duties.
 - Their amount and ex post distribution should not be determined until the close of

the financial year; when the company verifies it has attained the economic and financial indicators that justify their payment.

- Plan for the possibility of ex post adjustments and clauses of deferred payment, designed in a way that allows for one part of the variable payment to be delayed taking into account the appearance of contingencies not identified by the external auditor.

These assertions are applicable to all directors, regardless of their category. Thus, the compensation structure applicable to the internal or executive directors should be consistent with the Board of Director's remuneration policy. In addition, it should take into account their status as members of the company's senior management and be consistent with what is stipulated in the remuneration policy for members of the senior management, as will eventually be explained in this document.

In all cases, the remuneration policy for the Board of Directors and senior management should work to attract, retain and motivate professionals who have the capacity to make good contributions to the board and the senior management. It should be made public, known and duly explained to the shareholders, which means that it should be expressly approved by the Shareholders' General Meeting.

Other type of retributions, expenses assumption or lending should not be allowed, other than those approved in accordance with the remuneration policy. Thus, access to the means or goods of the company should not be allowed, nor the execution of transactions from which a non-justified benefit is obtained; it could be understood as an alternative form of obtaining payments by the directors or the senior management.

B. Transparency of the Compensation

Both the remuneration policy and the actual remuneration given to the Board of Directors and the senior management should be made **public and known to the shareholders** mandatorily, including the remunerative components on which the policy is based and the specific amount of remuneration for the board as a body and for the senior management.

The transparency of the compensation should be without any doubt a matter of obligatory compliance for listed companies and financial entities, which is why the legislator and regulator should incorporate it into the applicable norms.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
71. Adequate compensation for the Board of Directors	✓	✓	✓
72. Remuneration adjusted to performance	✓	✓	✓
73. Compensation policy approved by assembly	✓	✓	✓
74. Transparent payments	✓		✓

III.12. The organization of the Board of Directors (Guideline No. 29)

In this passage, we refer to the organization of the Board of Directors, detailing how the positions in its structure must be allocated to its members and to the committees, which it is advisable to

establish within the board. The organization of the board is particularly important, since it facilitates the involvement of the directors and the strengthening of their position before the senior management. It definitely enables the Boards of Directors to be active and empowered bodies, with the capacity to exercise this empowerment.

A. President or Chairman of the Board of Directors

The **president or chairman** of the Board of Directors should be **elected by the external members** of the board. The president may either be a patrimonial director – which in principle is the most usual practice – or an independent director. In any case this rule should apply to any kind of company.

This rule is based on the general principle of preventing the governing structure of the company from placing an excessive concentration of functions or powers in the hands of certain persons like the president (chairman) of the Board of Directors, its members and in particular, the Chief Executive Officer.

However, to limit eligibility for the president (chairman) of the Board of Directors to the external members of the same is a matter that has brought intense controversies in the different debates on Corporate Governance in recent times. This controversy is based on the multiplicity of corporate situations that exist in practice, so that in certain cases, the development of a company is not feasible without the leadership of a Chief Executive Officer who is also the president (chairman) of the Board of Directors.

There is no doubt that allowing a person to hold several positions may bring undoubted advantages to the company; in addition to clear leadership that allows for more efficient decision-making than when there is a separation of powers, and the agile transmission of information between the management of the company and the board. Nevertheless, the risks entailed in this accumulation of powers are evident. It has been empirically shown that companies with a single leader are more inclined to irregular practices that may end in financial scandals. This is fundamentally due to less independence of the board compared to the senior management, and consequently, less effectiveness in complying with its functions of supervision and control of the day to day management.

Therefore, the possible advantages deriving from the accumulation of positions in the company should not stop us from recommending that the best option is the **separation of the positions of president (chairman) of the board and chief executive**, even though separating them is not the usual practice in many countries.

Nevertheless, if the company has reasons for justifying that the president (chairman) of the board position should overlap with the Chief Executive Officer position, it should avoid concentration of power. It should also establish the necessary counterweights of power; like for example, when external members choose a vice-president of the board, preferably from the group of independent directors, the position adds certain functions related to the dynamics of the Board of Directors.

In general, we believe that with certain exceptions the position of the president (chairman) of the

Board of Directors is very weak in the countries of the region; the role is limited to overseeing the discussions in the Board of Directors and complying with the formalities laid down in the legislation in force. The presidents (chairmen) of the board do not usually act as leaders of the board, and in our opinion, is one of the main reasons why many Chief Executive Officers come to exercise a very strong influence on the Board of Directors. Sometimes it reaches the point of neutralizing their functioning and placing at risk the effectiveness of the system of controls and counterweights among the different levels of governance.

The statutes should stipulate the powers of the president (chairman) of the Board of Directors. The Guidelines propose **strengthening the functions of the president (chairman) of the Board of Directors**, among which the following stand out:

- Ensure that the Board of Directors establishes and efficiently implements the strategic direction of the company.
- Drive the governing act of the company forward, acting as a link between the shareholders and the Board of Directors.
- Coordinate and plan the functioning of the Board of Directors through the establishment of an annual work plan, based on the assigned functions: call meetings, prepare the agenda of the meetings (in coordination with the Chief Executive Officer, the secretary of the board and the other directors), present information to the directors in a timely and formal manner, preside over and lead discussions, ensure that the agreements of the board are implemented and follow up the recommendations of the Board of Directors, etc.
- Monitor the contribution of the directors and the annual evaluation of the Board of Directors and the committees.
- Undertake a certain degree of institutional representation in coordination with the Chief Executive Officer.

Additionally, the regulations of the Board of Directors should allow for a broad field of action in the development of the sessions of the Board of Directors, other than discussing the aspects found on the agenda, will deal with all those the president (chairman) brings up on his own initiative or those proposed by two or more of the directors, even if they are not included on the agenda of the meeting.

In most cases, and precisely due to the status as an external director, the president (chairman) will usually be responsible for presiding over the general shareholders meetings. As a consequence, the **president (chairman) of the Board of Directors should be given a different treatment** from the other directors in term of his/her commitment and dedication, and his/her compensation.

We believe that the **president (chairman) of the Board of Directors should not have a casting vote**. The by-laws may grant the president such a vote in highly exceptional situations, derived from vacancies on the board not covered by deputies on which the number of members is even making it impossible to reach agreements. This may be possible as long as it is not forbidden by the laws in force.

B. Vice-President of the Board of Directors

The Board of Directors may nominate one or several vice-presidents among its members whose functions allow him to serve as a replacement for the president. In our opinion, it is highly recommendable that this vice-president is also an external member of the board of the directors as a mechanism for a counterweight power, in a similar form as the president, but with more emphasis if the president is executive. **The company's by-laws should establish such a position and outline his functions**, as well as the conditions in which he/she may replace the president.

In general, the functions of the vice-president should not be limited to always acting as a replacement, and should be more important when the president of the Board of Directors is the Chief Executive Officer of the company, a situation in which in any case he/she may, on his/her own initiative, summon the Board of Directors, authorize the summoning of the Annual General Meeting, hold meetings with the independent directors, and lead the process for evaluating the president of the board.

C. Secretary of the Board of Directors

There is no doubt that the position of **secretary of the Board of Directors, who enjoys a certain autonomy** in his/her work, is very important for strengthening the functioning of the Board of Directors, in accordance with the internal and external norms applying to the company. Given the secretary's important functions, it is a good practice of Corporate Governance to enable him/her to have a direct line of communication with the board, and likewise to ensure that the procedures for his/her appointment and termination by the Board of Directors are especially rigorous.

This approach clashes with the tradition of all the countries of the region. The secretary is merely attributed with a status of the person who drafts the minutes, in accordance with the general tone of the agreements made by the board, and without any possibility to determine the legal validity of the adopted agreements. Both the by-laws and the regulations of the Board of Directors should establish **the rules for appointing the secretary and his functions**, among which these are recommendable:

- Guard the social documentation of the company, faithfully record the proceedings of the sessions in the minutes' book and testify to the agreements of the social bodies.
- Watch over the formal and material legality of the work of the Board of Directors and guarantee that its procedures and rules of governance are respected and periodically reviewed.
- Confirm that the work of the Board of Directors conforms to the by-laws, complies with the stipulations set forth by the regulatory bodies and takes his/her recommendations into account, and safeguard the observance of the principles or criteria of Corporate Governance accepted by the company and the norms in the regulations of the Board of Directors.

The secretary should guarantee compliance with the formal and material legality of the requisites laid down for the board's summoning, constitution and decision-making process, and also safeguard compliance with the company's procedures and rules of governance.

The Board of Directors may appoint a vice-secretary to assist the secretary and undertake his/her functions when he/she is absent. Given the nature of the functions performed, it is advisable that the vice-secretary be an expert in law. The secretary, who may or may not be a member of the Board of Directors, should help the president in his/her work and be granted independence in the exercise of his/her functions, and in any case, the appointment and termination will depend on the Board of Directors itself.

Due to the importance of the functions of the secretary, in terms of guaranteeing the legal, statutory and regulatory norms, it is highly convenient for the secretary to have a certain independence and stability. This way both his/her appointment and termination process would be a matter of special consideration on the part of the Nominations and Remuneration Committee.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
75. President (chairman) of the board chosen from the external members.	✓	✓	✓
76. Separation of the positions of the president (chairman) of the board and the Chief Executive Officer.	✓	✓	✓
77. Strengthen the functions of the president of the board (chairman)	✓	✓	✓
78. Differentiated treatment of the position of the president of the board (chairman)	✓	✓	✓
79. The President (chairman) should not have a casting vote.	✓	✓	✓
80. By-laws should stipulate the position of vice-president of the Board of Directors.	✓	✓	✓
81. Strengthen the position and independence of the secretary of the board.	✓	✓	✓
82. By-laws should stipulate the appointment and functions of the secretary of the Board of Directors.	✓	✓	✓

III.13. The Chief Executive Officer and the Senior Management (Guideline No. 30)

The best organization of good Corporate Governance requires the establishment of a **separation between the administration or governance of the company (represented by the Board of Directors) and its day to day management (responsibility of the senior management headed by the Chief Executive Officer).**

Consequently, the policy of the Board of Directors in general should delegate the day to day management of the company to the management team and focus its activities on the general functions of strategy, supervision, governance and control. The separation between administration and day to day management becomes the ideal formula and ensures that each body fulfills its function with the maximum effectiveness. This way, the directors are responsible for the control and vigilance

of the company by ensuring it is being directed effectively. The actions of the management, as the professional executives, should not be altered by interventions or acts of co-administration of the Board of Directors.

Nevertheless, the separation between day to day management and governance or administration should have some limits; the executive wing should in no case adopt measures or make decisions without the control of the Board of Directors. The Chief Executive Officer is the person responsible for the performance of the company's business dealings and for executing the guidelines and corporate strategy approved by the Board of Directors.

For that reason, the Chief Executive Officer should be granted the power to exercise the higher scrutiny of the administrative services and his/her general functions may be established in the by-laws. In any case, for every type of company, we recommend there is a clear policy for the delegation of functions by the Board of Directors and/or a definition of powers that allows for the delimitation of the empowerment of the Chief Executive Officer.

It has been frequently debated whether a Chief Executive Officer should be part of the Board of Directors. There is a widely held view that argues the Chief Executive Officer should not be part of the Board of Directors. However, in our opinion, the most consistent solution with the one-tier system of the administrative body found in all the commercial laws of the countries on the region is that the **chief executive should belong to the Board of Directors**. This is a way of guaranteeing that he/she is close and knowledgeable about the company's affairs and should have the status of an internal director, even in cases where the Chief Executive Officer is a significant shareholder of the company.

Nevertheless, our recommendation is that the Chief Executive Officer should not be appointed as the president (chairman) of the Board of Directors, as previously described in this section. The appointment of the Chief Executive Officer corresponds to the Board of Directors and must be adjusted to a number of rules and procedures similar to the ones used for proposing members of the Board of Directors. Nonetheless, it is much more usual to rely on the services of firms specializing in the selection of executive personnel (headhunters) when filling this executive position.

In the same manner, the Chief Executive Officer will be subject to the same selection and proposing regime by the Nominations and Remuneration Committee, or the Board of Directors in its absence, as well as to the duties of the members of the Board of Directors.

In every type of company, the Board of Directors should lead the **annual evaluation of the performance of the Chief Executive Officer**. On occasions, this practice, which should be undertaken in accordance with widely accepted methodologies, brings up situations which are difficult to treat: when the position of Chief Executive Officer is held by a shareholder or, in the case of closed companies of a family nature, when this position is held by a member of the family or relatives who are shareholders.

As for the Chief Executive Officer's termination, we believe that as a proposal of the Nominations and Remuneration Committee, or the whole Board of Directors in its absence, the board itself should be given the power to remove the Chief Executive Officer at any moment, without the need to explain any of the termination causes applying to the directors. As in the case of the directors, the Chief Executive Officer's remuneration is a subject that has been generating a lot of controversy lately.

Leaving aside questions of ethics and only from the standpoint of sound governance, it does not seem acceptable that chief executives receive exaggeratedly high retributions while the profitability of the shareholders decreases in terms of the dividends received and the value of their shares. What is more alarming yet is that year by year, the earnings per share of the shareholders continue to fall, while the overall remuneration package of their chief executives rises in net terms.

In this scenario, the remuneration of the members of the senior management has been one of the matters that has experimented the greatest development in recent years, especially in view of the scandals that surfaced after the outbreak of the global financial crisis of 2008.

Different recent studies allow to affirm that the variable component of the retribution of the chief executives is the source of this anomalous situation; the design of these variable components is based on the attainment of short-term benefits and include incentives for assuming risks which go beyond the appetite for risk found in the company's strategy (cash bonus, stock options).

In this context, the Guidelines propose that the **compensation of the chief executive should include a fixed and a variable component**. However, a company should avoid a situation where the variable component comes to "n" times the base salary or fixed component of the payment of the chief executive due to its design and calculations methods.

For that reason, the design of the **variable component should avoid a short-term view** and turn into a tool for aligning the interests of the Chief Executive Officer with the interests of the shareholders. Along these lines, the methodology for designing incentives in the remuneration of the chief executive should take into account adjusting the benefits for the company to the risks and capital cost, and the time horizon of the expected benefits as far as possible.

That is why the company should define a **Remuneration Policy for the Senior Management** that may be applied to the Chief Executive Officer and the members of its senior management and that considers the following aspects:

- The total compensation should include adequately balanced fixed and variable components.
- It is especially important that the fixed component is sufficiently important to allow for a special flexibility in the design of the variable component. It should also recognize the effective level of responsibility of each member of the senior management, the professional path in the company and the actual dedication, comparable with that of similar companies.
- The total compensation should reflect the results of the entire company and not be solely linked to the results of a single unit or business line.

- The total remuneration should take into account the creation of long-term value and reward the results on the basis of a prudent and responsible assumption of risks.
- The variable component in particular should be based on the attainment of objectives already established, prudent risk management, and take into account incentives adjusted to the long-term interests of the company that consider current and future risks.

For this, we propose that:

- As possible, the variable component should be awarded ex post, that is, after the end of the financial year, when it becomes possible to verify whether the economic and financial indicators have been attained and the assumed risks have been maintained to acceptable levels in terms of risk-tolerance.
- The above assumes the inclusion of deferral clauses, designed in a way that a substantial part of the variable remuneration is subject to a deferred payment, taking into account the economic cycle, the nature of the business and its risks.
- Plans should be made for the possible existence of ex post adjustments of the variable component deriving from the establishment of clauses that prevent or limit the payment of the deferred variable remuneration; for example, in the face of changes in the balance sheet determined by the external auditor.
- In terms of the variable component, the compensation scheme for control functions personnel and those not directly linked with the business should exert greater weight in the objectives related to their functions; these should help strengthen their independence in the business areas that are effectively controlled.
- The variable component should seek a balance between the amounts to be paid in cash and those to be paid in the form of shares or financial instruments, which may reach 50%. Payment in shares should be subject to deferrals, for example, of one year.
- The variable component should be adequately explained to the shareholders. The existence of complex schemes that are difficult for the shareholders to understand has caused on various occasions undesirable and unforeseen levels of compensation for the senior management.

Finally the existence of golden parachutes for the Chief Executive Officer and other members of the senior management must be linked with the actual performance of the company and must be formally approved and moderated by the Board of Directors. It will also be subject to a prior report from the Nominations and Remuneration Committee, and even approved by the assembly, to avoid the emergence of abusive or unjustifiable situations.

When the indemnification commitments in these kinds of clauses surpass certain amounts (for example, three annual salaries of the executive), the surplus should necessarily be provisioned in the balance sheet of the same financial year in which it was approved, detailing the amount as a separate item.

If the shareholders agree there are reasons for which the CEO could not be part of the Board of Directors, he/she will have the duty to assist to the board's sessions without a voting right as re-

quired by the board and excluding those sessions where his/her performance is evaluated. This way the Chief Executive Officer can provide the board with information regarding the different items on the agenda or any pertinent subjects.

The senior management of the company is made up of a group of people with technical and executive experience who usually report directly to the Chief Executive Officer. The members of the senior management may be selected, evaluated and appointed by the Chief Executive Officer, since they will clearly be direct collaborators in the day to day management of the company. However, from the perspective of Corporate Governance, it is also perfectly permissible that the executives of the company are appointed by the Board of the Directors, following the proposal of the CEO.

In any case and regardless of who makes the final appointment, the candidates for executive positions in the company should be examined and evaluated by the Board of Directors' Nominations and Remuneration Committee, which should publish its opinion or that of the entire board.

We recommend that for every type of company the termination of senior executives should be the exclusive responsibility of the Chief Executive Officer, and not of the Board of Directors, even in cases when the latter has been given the power to appoint them. This is due to the urgent nature any decision to lay off an executive can have, which does not justify having the board to make the decision at the suggestion of the Chief Executive Officer. In any case, the Board of Directors should quickly be informed of the termination of any of the senior executives.

Finally, as in the case of the CEO, the performance of the members of the senior management should be evaluated annually and the results shared with the Nominations and Remuneration Committee, or the Board of Directors in its absence.

KEY RECOMMENDATIONS	Recipients		
	Listed	Non Listed	Financial Entities
83 Separation between the administration and day to day management	✓	✓	✓
84 Chief executive as a member of the Board of Directors	✓	✓	✓
85 Senior management's Compensation Policy.	✓	✓	✓
86 Variable component not based on a short-term view and is aligned with current and future risks.	✓	✓	✓
87 Evaluation of the performance of the CEO.	✓	✓	✓

III.14. Dynamics of the Board of Directors (Guideline no. 31)

To enhance the efficacy in the Board of Directors' functioning, it is necessary that its Regulations establish the rules for its summoning, the frequency of its meetings and the procedures for its development, among other matters.

It is clear that in many companies in the countries of the region, the Boards of Directors do not adequately fulfill their functions because their meetings are not systematically organized and in many cases they act as true “paper directors”.

In every type of company, the president (chairman) of the Board of Directors, with the assistance of the secretary and Chief Executive Officer, should propose a **work plan** of the Board of Directors for the financial year. It should be based on the set of functions assigned to the administrative body and their complexity and recurrence. This will clearly help determine the most reasonable number of ordinary meetings per year.

It is very difficult to come up with a specific figure for the ideal number of meetings per year, since it depends on multiple factors: the complexity of the subjects under discussion, the company’s situation at the time, its regional presence, the structure of the Board of Directors and other variables that should be taken into account when preparing the work plan.

However, the example of both, the boards that meet too many times (for example, more than once a month) and those that meet too sporadically (for example, four times per year) lead us to think that either their functions are not well defined and they are falling into the error of co-administration, or, on the contrary, they are acting as formal directors, without a real content.

Consequently, we believe that for listed companies and financial entities, the most reasonable number of meetings should be between eight and twelve times per year, while for closed companies that are not especially complex, this figure may vary between six and ten meetings per year.

We likewise recommend that for any type of company at least **one or two meetings per year should be clearly focused on strategy**. The experience of many companies shows that it is best for these kinds of meetings focused on strategy to be held outside of the company’s headquarters (“off-site” meetings).

Given the board is required to **meet at regular intervals**, at the beginning of each year the Board of Directors should approve a **concrete timetable for the ordinary sessions** in the course of that year, without jeopardizing its right to call as many extraordinary sessions as necessary. Furthermore, we believe that the practice of holding meetings without the presence of the board members (where they communicate by written, electronic or other indirect means) should be limited to cases where reasons of necessity or urgency justify it.

Likewise, **the president (chairman) should call for a meeting of the Board of Directors upon the request of two or more directors, or the Chief Executive Officer.**

As already pointed out previously, the call for the assembly must be accompanied by the provision of the relevant documents or **sufficient information** to make the work of the Board of Directors more effective through the active participation of its members. This will allow the directors to take their decisions in a reasoned and justified manner.

In this sense, the president (chairman) of the Board of Directors should assume the responsibility that directors receive the information with sufficient time in advance of the meeting itself and ensure

that the **information is useful**; quality should be more important than quantity in the documents delivered to the directors.

In compliance with the commitment acquired by the company and, in particular, with its shareholders, the directors must assume the responsibility of studying the documents they have received in advance of the meeting. They should understand that the objective of the meeting of the board is to deliberate and take decisions; it should not be as an occasion to obtain general information about the company, even if it has already been sent.

Therefore, a president of the board (chairman) who is experienced and fully fulfills his/her functions will not find it difficult to monitor how diligent the directors have been at studying the documentation they received for the meetings and, in each case, he/she should act accordingly.

The agenda of the meetings of the board, for which the president (chairman) and not the CEO is ultimately responsible, should be structured in accordance with certain parameters allowing for a logical order in the presentation of the subjects and the discussions.

The attendance of the titular directors to the sessions of the board is regarded as a fundamental aspect of Corporate Governance, insofar as the commitment they have assumed towards the shareholders, implies contributing with their knowledge, experience and background to the company. As a consequence, their attendance to the meetings is a further expression of their duty to be diligent. For that reason, the company should **publish in the annual report and on the corporate website, if applicable, the record of the directors' attendance to the sessions** of the board of the directors and to the committees they assist.

Finally, at least once a year, the Board of Directors should **evaluate the effectiveness** of its work as a collegiate body, the reasonability of its internal norms and the dedication and performance of its members, proposing, when necessary, any modifications of its organization and functioning which are regarded as relevant.

In evaluating the Board of Directors, it is recommendable that for every type of company, the methodology of self-evaluation is alternated with an evaluation made by external consultants. The evaluation of the board is a complex, but necessary, sensitive process. It is complex because the evaluation reviews aspects concerning both the Board of Directors itself and even every director on an individual basis. It is sensitive, since it is a matter of analyzing the exercise of the real power of the board. In many occasions it may cause tensions among its members, even more when an evaluation of the specific performance of the directors on an individual basis is undertaken.

The Board of Directors is evaluated from its composition as a body analyzing the group of profiles represented in relation of the necessities on each moment, the focus of the attributed functions, the dynamics of its act (the development of the sessions, their frequency and duration, the treatment and handling of the agenda and depth of the discussions), the significance and contribution to value of the constituted committees (when they exist), the quality of the information received. In short, it analyzes the effectiveness of its work as a collegiate body.

For its part, the individual evaluation of the directors has a direct impact on their actual remuneration and in many occasions affects their re-election. It should analyze both the profile of each director, and his/her performance in the board and the value added by completing the tasks of his/her position.

The development of the evaluation allows the company to obtain feedback on the labor realized by the board during a given period in terms of exercising their responsibilities. This evaluation enables the company to identify the strengths, level of efficiency and opportunities for improvement of the Board of Directors, its committees, and its individual members.

Consequently, this practice is very beneficial in strengthening the work of the Board of Directors, the committees and its individual members; it is just recently that companies are starting to do this evaluation on a periodical basis.

The evaluation of the Board of Directors should ideally be undertaken by an external firm which specializes in that field. It will usually include both questionnaires and questions for individual meetings with the directors, and the analysis of written information, so that integral results of maximum value to the company may be obtained.

However, it may likewise be interesting for the company, and of course less burdensome, to make a cross-comparison between the evaluation done by an external firm and a self-evaluation made by the board itself, based on the questions and methodology of the external firm.

In any case, the company should always avoid exercises of self-evaluation done by the Board of Directors itself as they are usually not familiar with the methodology. The sensitive and complex nature of this process makes it advisable to resort to external professionals on a periodical basis to ensure the evaluation will be valuable to the company.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
88. Work plan for the board	✓	✓	✓
89. Periodical meetings of the board.	✓	✓	✓
90. Concrete calendar for the ordinary sessions	✓	✓	✓
91. Meetings with a strategic focus.	✓	✓	✓
92. Summoning of the Board of Directors by directors or CEO	✓	✓	✓
93. Delivery of sufficient and useful information.	✓	✓	✓
94. Disclose the attendance record of the directors.	✓	✓	✓
95. Evaluation of the Board of Directors.	✓	✓	✓

III.15. Committees of the Board of Directors (Guideline no. 32)

The Board of Directors in every type of company may create **internal specialized committees** to act as support and study bodies. These committees can be temporary or permanent and will have the capacity to present proposals to the board and eventually exercise certain delegated functions.

Currently, the most common permanent committees are the **Auditing Committee and the Nominations and Remuneration Committee**. Given the characteristics and complexity of their business, companies should take advantage of the opportunity to provide themselves with a **Risks Committee**. It must be noted that the non-existence of these committees does not mean these functions are not carried out; they always remain under the scope of analysis of the Board of Directors.

From our perspective, forming an Auditing Committee should be obligatory by regulation or law to listed companies and financial entities, as in fact occurs in several countries of the region. In the case of financial entities, regardless of their size, the existence of a Risks Committee should also be obligatory. Companies not listed should base the need to create or not create these committees on their circumstances, size and complexity. These committees should be regarded as an extension of the Board of Directors itself and thus, should not be regarded as committees on a management level.

Consequently, they are made up of **external directors**, with a significant presence of independent external directors. Given their character as support and study bodies, they will have the capacity to inform and make proposals to the Board of Directors on the matters they are responsible for, which are usually complex and of a technical nature; the board may eventually ask them to decide on certain questions.

The regulations of the Board of Directors and/or the regulations of each committee should ensure that the committees permanently inform the board of the development of their tasks, as well as the procedures and frequency of the information the presidents of the committees should supply to the Board of Directors.

A. Auditing Committee

The Auditing Committee should be composed of a minimum of three and a maximum of five **external directors**. When the company has a commissioner, fiscal auditor or trustee, they can be invited to participate in the meetings, but without a voting right.

With the objective of making the Auditing Committee more dynamic, especially in the beginning phase, the company can count on the stimulus and support of high-level guest executives experienced in the matters the committee deals with. The person responsible for the internal auditing unit and the regulatory compliance unit should be included among these guest executives.

The Board of Directors will be the body that determines the exact number and appoints the members of this committee. For this, the board should take into account their knowledge and professional experience in banking, finance, auditing, accounting and other similar fields. According to their experience, they should be able to read and understand financial statements of similar scope and complexity to those of the company. Their termination should be done following a proposal by the Nominations and Remuneration Committee.

The members of the committee shall leave their positions when they cease to be directors of the company or when the Board of Directors decides it. Notwithstanding the above, it would be logical

to establish a maximum term of office for the president of the Auditing Committee. We propose that he/she should be replaced after a time set by the by-laws or the regulations of the Board of Directors, which we believe should not be longer than five years, allowing for his/her eventual re-election after a suitable lapse of time, for example two years after his/her termination.

The main task of the Auditing Committee will be to assist the Board of Directors in its oversight functions, through the evaluation of accounting procedures, the relationship with the external auditor and a review of the company's control structure.

In concrete terms, the Auditing Committee shall have the following responsibilities, among others:

- Inform the Annual General Meeting on questions related to the responsibility of the Auditing Committee.
- Propose to the Board of Directors and eventually to the Annual General Meeting, the appointment of the external auditor and the conditions of his employment, and when necessary, its revocation or non-revocation.
- Supervise the activities of the external auditor.
- Be responsible for relations with the external auditors, act as their counterpart and especially, evaluate all matters that could put the committee's independence in jeopardy. The Auditing Committee must also overview the external directors in other issues related to the auditing plan and the development of the accounts audit as well as other communications stipulated in the legislation on the account auditing and the technical norms of accounting.
- Receive the final report of the external auditors. In case they contain any reservations or exceptions, the Auditing Committee should be able to explain its content and scope to the shareholders. If it is a listed company or registered as an issuer of securities in capital markets as well, the Auditing Committee should verify that the senior management takes the recommendations of the external auditor into account, and when appropriate, lead the process of responding to the observations which the external auditor includes in their letter to the management.
- Ensure that the accounting criteria currently in force are properly applied to the financial statements the Board of Directors presents to the General Meeting. It should also procure that the company is in close touch with the processes of implementation, on a national or sectorial level, of the international norms on financial information (IFRS/IAS).
- Investigate and evaluate the process of financial information.
- Supervise the functioning of the company's website and other mechanisms for disclosing information.
- Oversee compliance of the regulations and legal requirements.
- Verify that all of the periodical information offered to the markets is drafted in accordance with the same principles and professional practices that apply to the annual accounts, always supervising this information before it is published.
- Investigate and evaluate the company's systems of internal control.

- Supervise and present periodical reports on the application of the company's risks policy, so that the main financial and non-financial risks, whether seen on the balance sheets or not, are identified, managed and suitably disclosed.
- Supervise the activities of internal auditors.
- Propose to the Board of Directors the selection, appointment, re-election and termination of those responsible for the company's internal audit.
- Review the annual work plan of the internal auditors and the annual report on its activities.
- Ensure the independence and effectiveness of the function of the internal auditors, receive periodical information on their activities and verify that the senior management takes the conclusions and recommendations of their reports into account.
- Review compliance with the actions and measures that result from the reports or inspection activities of the authorities for supervision and control.
- Inform the Board of Directors of the following company operations before their approval: directly or indirectly, with directors, significant shareholders or those represented on the Board of Directors, or members of the senior management and on intra-group operations or persons linked to them.
- Monitor regularly the degree of compliance with the code of ethics and the effectiveness of the system of whistleblowers evaluating any unethical activities that may arise, the content of the complaints filled and making the relevant recommendations to the Board of Directors.

B. Nominations and Remuneration Committee

The Nominations and Remuneration Committee should be integrated of a minimum of three and a maximum of five External Directors. With the objective of making the committee more dynamic, especially in its initial phase, it is recommended the stimulus and support of high-level guest executives with experience on the matters that pertain to it, among which should be included the company's head of human resources.

The Board of Directors will set the specific number; will appoint and will dismiss the members of this committee. The board should take into account the knowledge and professional experience in human resources, Corporate Governance, banking, payment systems and similar matters, of the members. The members of the Nominations and Remuneration Committee will need to have a sufficient level to understand the scope and complexity of the matters for the company.

The main task of the committee is to help the Board of Directors in its functions of appointing, re-electing, dismissing and paying the directors and the senior management of the company, authorize and report on transactions with linked parties and oversee the observance of the governance rules of the company, periodically reviewing compliance with such rules, recommendations and principles.

Concretely, the Nominations and Remuneration Committee should assume the following responsibilities, among others:

- Inform the Annual General Meeting about their activities and the questions pertinent to their functions that the shareholders may raise.
- Evaluate periodically the skills, knowledge and experience required by the board.
- Propose and review the criteria that should be followed for the composition of the board and the evaluation of candidates.
- Inform on the suitability of the possible candidates to the Board of Directors, so they can be proposed to the Annual General Meeting by the board or directly by the shareholders.
- In cases of the re-election or ratification of the directors, the committee will formulate a proposal that contains an evaluation of the proposed director's work and actual dedication to his position during his most recent period as a director.
- Inform the board of those directors that could negatively affect the work of the board or the credit and reputation of the company, particularly, when they have violated one of the legally established principles of incompatibility or prohibition.
- Examine and organize the process of succession or replacement in a planned manner on hypothetical situations of termination or resignation, illness or death of the members of the board or of their committees.
- Examine and organize the process of succession or replacement in a planned manner on hypothetical situations of termination or resignation, illness or death of the company's Chief Executive Officer and other members of the company's senior management and key executives, by formulating the corresponding proposal to the Board of Directors.
- Propose the directors' compensation policy and the senior management compensation policy to the Board of Directors, which should be approved by the assembly.
- Within the framework of the compensation policy approved by the Annual General Meeting, propose to the board the individual amounts of payments of the directors, including the president, and , if they exist, internal directors; this regarding to their performance of functions other than those of the Board of Directors and other stipulations of their contracts.
- Safeguard the observance of the policy of remuneration of the directors and the transparency of their remunerations.
- Periodically review the directors' and senior management's compensation programs and make pertinent recommendations to the Board of Directors.
- Formulate the annual report for the directors' and senior management's compensation policy.
- Propose the company's Human Resources policy.

C. Risks Committee

In most types of companies the Board of Directors usually has the responsibility for understanding and monitoring each of the risks to which the company is exposed and the techniques used for their measurement and administration. In most companies the board also approves the general policy on risks and reviews the information provided on risks by the senior management . However, the particular characteristics of the company may justify the need for the establishment of a specialized

Risks Committee by the Board of Directors. In the case of financial entities, the creation of the Risks Committee should be imperative.

The Risks Committee should be made up of a minimum of three and a maximum of five **external directors**. To make the committee more dynamic, especially in its initial stage, it may count on the stimulus and support of high-level guest executives, with experience in the matters the committee is responsible for, among which the Chief Risk Officer (CRO) or an equivalent position should be included.

It will be up to the board to set the specific number and appoint the members of the committee. The board should take into account the knowledge and professional experience in banking, risk management, finance, auditing and similar fields of the members, and make sure they have sufficient experience to understand the scope and complexity of these matters pertaining to the company. The board shall also be responsible for the termination of members of that Risks Committee.

The ultimate function of this committee is to support the Board of Directors in the fulfillment their risk management responsibilities, through the periodical undertaking of the following tasks.

- Review and evaluate the integrity and suitability of the company's function in risk management.
- Review the adequacy of the economic and regulatory capital of every company and its allocation to the different business lines and/or products.
- Review the limits and reports about risks, making the relevant recommendations to the board.

In concrete terms, the Risks Committee should assume the following responsibilities:

- Inform the Annual General Meeting about its activities and deal with the questions in its area of responsibilities which the shareholders set forth in the assembly.
- Propose the company's risks policy to the Board of Directors.
- Systematically evaluate the company's risk strategy and general risk policies, translated into the establishment of limits in terms of risks and business activity, broken down into business dealings, corporate or economic groups, clients and areas of activity.
- Analyze and evaluate the day to day risk management in the company in terms of limits, risk profile (expected loss), profitability and capital maps (risk capital).
- Analyze and evaluate the systems and tools used for risk control in the company.
- Formulate improvement initiatives for the control and risk management internal systems.
- Raise to the Board of Directors proposals of norms to delegate the approval of the different types of risk that the board or lower levels of the organization can assume.
- Inform the Board of Directors about operations it can only approve, that are above the delegated responsibilities of lower levels or bodies.
- Evaluate and follow up the indications laid down by the supervisory authorities for the performance of its work.

- Impulse the adjustment of the company’s risk management to an advanced model that allows for the configuration of a risk profile aligned with the established objectives. The committee should also follow-up the degree of adjustment of the risks assumed in that profile.

Complementary to this, CAF – Development Bank of Latin America – in collaboration with the Economic Commission for Latin America and the Caribbean (ECLAC) and the Inter-American Development Bank (IaDB) elaborated the document “*Corporate Governance in Brazil, Chile, Colombia, Mexico and Peru: The determinants of risk in corporate debt issuance*”, that proposes the creation of a **committee of investments in financial assets** for companies which issue debt securities. The authors of the document assesses this committee of investments would be responsible for structuring the strategy for investment in financial instruments and providing information about the same, as well as a **committee on corporate finance**, that would be responsible for analyzing and informing a company about its financial needs and the different alternatives that exist.

The decision to establish or not these two very specialized committees will also depend on the size of the Board of Directors. It also has to do with the degree of complexity and degree to which a company’s financial investments and corporate finance can affect the value chain of its activities. In any case it would only apply to especially complex financial entities or listed companies of a large size. For the rest of the cases, its functions may be directly undertaken by the Risks Committee, in most cases, or the entire Board of Directors.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
96. Specialized committees	✓		✓
97. Committees made up of a majority of external members	✓		✓

IV. Control Structure

Control structure is an integral concept that brings together everything related with the subjects of control structure, risk management, internal control systems, information and communication, and monitoring.

Basically, control structure is the integral system that enables the company to count on a structure, policies and procedures undertaken by the entire company (from the Board of Directors and senior management down to the employees themselves) and provides a reasonable security when it comes to achieving the objectives of the company.

Control structure should be in line with the treatment of this subject found in COSO (*Committee of Sponsoring Organizations of the Tradeway Commission*) that establishes the main guidelines for the introduction, management and control of a system of internal control (COSO I) and administration of risks (COSO II).

Among the main benefits of the COSO are the following:

- Facilitates the incorporation of consistent and aligned procedures.
- Improves the follow-up of the performance related to the strategic objectives.
- It strengthens the capacity to manage the risks necessary for the business strategy in an appropriate way.
- It facilitates the understanding of risks in decision-making processes.
- It strengthens the control of the combination of risks to which the organization is exposed.

In accordance with COSO, the control structure may be broken down into five major components.

- 1. Control Environment:** understood as the tone of the organization in terms of risk management and control, and it is thus related to its philosophy of risk and control management, the definition of structure (roles and responsibilities), ethical values, and in short, the environment of the organization related to risk management and control.
- 2. Risk Management:** understood as the treatment of the assessment and management of the organization's risks, which includes:
 - The establishment of objectives to be achieved (strategic, operations, report on financial and non-financial information, and compliance).
 - Identifying events that may (positively or negatively) affect the achievement of the objectives.
 - The evaluation of risks (probability and impact), by means of which the potential events may affect the objectives of the business.
 - The response to risk; fundamentally a question of avoiding, mitigating, sharing or accepting risk.
- 3. Control activities:** policies and procedures that help the management ensure the responses to risks are undertaken in an appropriate and timely manner.
- 4. Information and communication:** the communication throughout the entire organization needed for the functioning of the entire control structure.
- 5. Monitoring:** Evaluation to ensure the effective functioning of the control structure.

As a general rule, any company has control and risk administration systems that are sometimes complemented by external systems of control employed by different entities (an external auditor or supervisor in the case of supervised companies are the most common examples). However, these controls do not always operate systematically, and more preoccupying, they do not always safeguard the interests of the company subject to control.

Evidently, the availability of a modern and efficient control structure implies a cost of a certain dimension for the company. Nevertheless, we believe that its importance for the creation of solid and trustworthy information is such that considerations of cost should not take precedence over the existence of a solid control structure. In the end, it also makes the financial and non-financial information which it provides reliable, ensures a reasonable security in the attainment of the objectives set by the company and allows for suitable responses to the expected or unexpected risks that may affect a company.

In fact, the existence of a suitable control structure is a key tool for the Board of Directors itself; with the availability of sound, high-quality information, the board may exercise its control over the company's senior management in a correct manner and supervise the security and trustworthiness of the company itself.

The intensity and complexity of the control structure will vary in accordance with such factors as the size and complexity of the business ventures or processes of the company, its geographical spread and, especially, the nature of the risks it faces. As a general principle in listed companies and especially, financial entities, the control structure that applies will be the most complex without a doubt, given that the business of the latter is based on the proper administration of risks.

IV.1. Control Environment (Guideline no. 33)

The control environment is the fundamental component in the control structure of any company. In a general manner, it defines the company's philosophy on the control and administration of risks, as well as the tone or importance which the organization gives to it. A correct control environment depends on an adequate philosophy and culture of risks and control in the company and it is the basic premise of an adequate control structure as a whole. The scope of control mainly affects:

- The philosophy of integrated risk management.
- The role of the Board of Directors in supervising the systems for managing risks and control.
- The integrity and ethical values of the company.
- The structure that is defined in the company for the integrated risks and control management, establishing roles and responsibilities, delegation policies and lines of reporting.
- The requisites and profiles required for risk management and control activities.

Therefore, it can be noted that the control environment is the cornerstone on which the entire architecture of control rests.

The **Board of Directors has the ultimate responsibility for the existence of a solid control environment** in the company, adapted to its nature, size, complexity and risks, so that:

- A culture of risks and control is promoted in the entire company reaching through the organization as a whole.
- Roles and responsibilities are defined for the management of risks, internal control and evaluation, with clearly defined lines of reporting.
- The risks deriving from the business processes and the definition of the strategy of the company are taken into account, in order to undertake its adequate follow-up, evaluation and management.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
98 Existence of a solid control environment adapted to the size and complexity of the company.	✓	✓	✓

IV.2. Risk Management (Guideline no. 34)

In general, risk management encompasses the definition of the risks policies, as well as the definition and execution of the processes for the identification, evaluation, administration, monitoring and reporting of risks.

Specifically, the objectives of risk management are:

- The identification of risks, as a consequence of the strategy defined by the company.
- The evaluation of risks and measurement of the degree of exposure to the same.
- The management of risks, which includes making decisions about handling risks (avoid the risk, mitigate it, share it or accept it).
- Monitoring risks by evaluating whether the decisions about assuming risks are in line with the risks policy (issued by the board) and within the maximum limits of exposure defined by the same.
- Reporting to the Board of Directors and senior management on risk management.

While this is a general framework, we usually find that the companies of the region, especially the ones not listed, still have a very basic structure for risk management.

From the practical point of view, companies not listed should have a “**risks map**”, understood as the identification and follow-up of the financial and non-financial risks to which the company is exposed (for example, market, credit, liquidity, business and reputational risks, etc.). This risks map, which in practice should be known to the senior management of any company, needs to be formalized and made known to the board. This way the board can be aware of all of the risks to which the company is exposed and supervise the concrete actions needed for the proper administration of such risks.

However, we believe that for listed companies, and especially financial entities, the time has come to **strengthen risk management** with a more solid and professional structure. In addition to a company's risks map – which should be fully aligned with the COSO– it should also ensure that:

- **The board** should be responsible for defining an **integral policy for risk management** and also set **maximum limits for exposure** to each identified risk. In addition, **the board should periodically examine and review the company's current exposure to the maximum defined risk limits, as well as to propose and oversee correcting and monitoring actions** in case of deviations.
- The **senior management** should be **responsible for the process of managing** risks that is, identifying, evaluating, controlling, monitoring and reporting the risks, defining the methodologies and ensuring that risk management is consistent with the company's strategy, its risks policy and maximum approved limits.
For this, there should be a **policy for the risks delegation**, approved by the boards, which establishes the risks limits, which may be directly administered by each level of the company.
- The business units or departments themselves should be instilled with a risk managing culture, which allows them to be aware of the risks generated by their own activities.

The responsibility involved in the process of managing risks lead us to put a high value on the position of the **risks manager**, who has the ultimate responsibility for managing the company's risks at the senior management level.

In our opinion, the establishment of this position is unavoidable for financial entities, given the complexity of the risks they manage. In the case of listed companies, however, and depending on their complexity, a gradual adoption of this position would be justified, temporarily assigning those functions to the company's Chief Executive Officer.

From the perspective of Corporate Governance, the risks manager should be a figure who has:

- A high internal status, sufficient resources for the exercise of his/her functions and defined responsibilities.
- A direct relation with the Chief Executive Officer and the senior management, since risks and business are two sides of the same coin.
- The capacity to influence the organizational decisions which affect the degree of exposure to corporate risks.
- Complete access, throughout the organization, to information needed for the exercise of his/her functions.
- Direct reporting lines to the Chief Executive Officer and the Board of Directors (or the Risks Committee in the companies which have one).
- A position strengthened by the fact that his/her appointment and termination is a decision of the board and does not have managerial responsibilities other than risk management.

KEY RECOMMENDATIONS	Recipients		
	Listed	Non Listed	Financial Entities
99. Existence of a risks map, known to and supervised by the Board of Directors	✓	✓	✓
100. Policy for risk management approved by the Board of Directors	✓		✓
101. Policy for delegating risks approved by the Board of Directors	✓	✓	✓
102. Senior management responsible for the process of managing risks	✓	✓	✓
103. Existence of a risks manager	✓		✓

IV.3. Internal Control System (Guideline no. 35)

For its maximum effectiveness and greatest value contribution, risk management requires a system of internal control meant to ensure that:

- Each of the identified risks in the different processes of the company is adequately managed in accordance with its risks policy and culture, so that there are a number of specific controls; as well as,
- The establishment of policies, processes and measures which are effectively applied in practice.

For that reason, the systems of internal control are a key factor in ensuring that the information on risks that reaches the board and senior management is:

- Reliable
- Truthful
- In line with reality

In short, internal control is nothing more than the set of specific policies, procedures and activities that help the senior management to ensure that responses to risks are implemented in a suitable and timely manner. For that reason, it is fundamental that **the board is responsible for overseeing an adequate system of internal control**, adapted to the company's own complexity and consistent with the risks management in force. The board should also **supervise its effectiveness and suitability**, which **can be delegated to the Auditing Committee**.

The internal control system should be the responsibility of the company as a whole in order for it to be consistent with the risks and complexity of the company. This leads us to the **principle of self-control**, understood as *"the capacity of the people engaging in the different processes to regard control as an inherent part of their responsibilities, fields of actions and decision-making"*. This is fully consistent with the COSO approach.

However, it should be reinforced with the existence of a person who is ultimately responsible for internal control, who enjoys a complete and integral view of the set of controls stipulated by the

organization, a responsibility which should fall to the risk manager, or in his/her absence, the Chief Executive Officer.

Naturally, the responsibility for evaluating and ensuring the implementation of the controls in force cannot lie in those who design the controls. It should be the exclusive responsibility of the internal auditor, who, in turn, may propose the necessary improvements to the Auditing Committee, as we shall explain below.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
I04. Board of directors responsible for overseeing an adequate system of internal control	✓	✓	✓
I05. Supervision of the effectiveness of the internal control system by the Board of Directors or Auditing Committee	✓	✓	✓
I06. Principle of self-control in the entire organization	✓	✓	✓
I07. Chief executive officer or risks manager responsible for the design of the controls	✓	✓	✓

IV.4. Information and disclosure of risk management policies and control systems (Guideline N°36)

An effective risk administration and internal control system requires, among other factors, an organizational culture in which both the senior management and the entire organization manages the risks generated by their own activities and design the relevant controls. For this reason, it is crucial that the culture, philosophy and policies of risk are disclosed top-bottom and horizontally across the entire corporation within the approved exposure limits. This way the entire organization will take risks and their control measures into account, when carrying out their respective activities.

Additionally, an efficient system for risk management and control requires that information should be reported bottom-up (towards the board and senior management) and that it must be trustworthy, comprehensible and complete, effectively supporting decision-making processes.

In short, listed companies and financial entities should count on **systems of internal information that support decision-making and risk management and control**. Every type of company should have a process of internal communication, which enables:

- The senior management to involve the entire company, highlighting its responsibility for the risk management and definition of controls.
- The company’s personnel to understand their role in risk management and the identification of controls, as well as their individual contribution in relation to the work of others.

This process of communication about risk administration and control should allow everyone in the company to be familiar with:

- A common language regarding risks.
- The risk limits tolerated by the company.

- The role and responsibility of every person in risk management and control.
- Acceptable and unacceptable behaviors.
- The existence of internal and external channels of communication.

In this context, an aspect of special importance for listed companies and financial entities is the convenience of having **internal lines for anonymous denunciations or “whistleblowers”**. These enable employees to report anonymously anti-ethical conducts or conducts that could violate the company’s culture of risk management and control. For financial entities banking regulators should include as a matter of obligatory compliance, the provision for these types of lines for anonymous complaints.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
I 08. Systems of information for risk management and control	✓		✓
I 09. Process of internal communication on risks and control	✓	✓	✓
I 10. Lines for anonymous denunciations or “whistleblowers”	✓		✓

IV.5. Monitoring the control structure

A. The duties of internal auditing (Guideline no. 37)

Monitoring is a fundamental component for the evaluation of the effectiveness of the control structure. So far, the responsibilities about the control environment, risk management and the internal control systems involve the Board of Directors, the senior management and the company as a whole.

Nevertheless, **the labor of monitoring**, that is, the evaluation of the effectiveness of the control structure, also involves both the **internal and external auditors**, as these are figures that listed companies and financial entities should count on. Monitoring is understood as providing objective assurance to the Board of Directors to ensure the effectiveness of risks management in an organization. This helps to ensure that key business risks are being handled appropriately and the internal control system is being operated in an effective way.

There has been a lot of controversy about the current scope of the labor of monitoring. It has been suggested, on occasions, that the internal auditors should have some kind of responsibility for the effective management of risks. However, this should not be their function, as they would lose their objectivity and independence when executing the labor of monitoring itself, which is their true responsibility. Rather, the responsibility for the effective management of risks must fall on the senior management.

In addition, there has currently been an important debate about the work of consultation that the internal auditors can do. In our opinion, while it is true that the internal auditors may act as consultants to the senior management defining and improving processes, certain precautionary measures or safeguards should be applied, like transferring the responsibility of these activities to the members of the senior management as soon as possible. In any case, we propose that listed companies and financial entities should have a **policy on internal auditing**, approved by the Auditing Committee, where the scope of its functions in this field should be expressly stated. It should include the following:

- The autonomy and independence needed to exercise their functions.
- The labor of evaluating and ensuring the implementation of the processes for risk management and for ascertaining that risks are correctly evaluated.
- An evaluation report for key business risks.
- A revision of key risks handling.

In order to carry out the functions mentioned above, it is crucial that the person with the **maximum responsibility for internal auditing** has a relationship of **professional independence** with the company that hires him/her by making him/her exclusively dependent of the Auditing Committee when exercising their respective functions of this position. The internal auditor should act in accordance with the same principles of diligence, loyalty and discretion required to the Board of Directors.

In addition, the responsibility for his/her **appointment and termination should fall on the board**, following a proposal from the Auditing Committee. The termination of the internal auditor assignment should be communicated to the stock market. With the aim of maintaining independence and autonomy, the **internal auditor's line of reporting** should respect the hierarchical principle, reporting to the **Auditing Committee**, and subsidiary to the Board of Directors.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
I 11. Involvement of internal and external auditing in the labor of monitoring	✓	✓	✓
I 12. Policy for internal auditing	✓		✓
I 13. Professional independence of the person ultimately responsible for internal auditing	✓	✓	✓
I 14. Responsibility of the Board of Directors for appointing and dismissing the internal auditor	✓	✓	✓
I 15. The line of reporting by the internal auditor should to the Auditing Committee respecting the hierarchical principle	✓		✓

B. The duties of external auditing (Guideline no. 38)

In addition to the labor of internal auditing, there is also an external perspective to monitoring, which corresponds to the external auditing firms. The appointment of the external auditors should follow a

proposal from the Board of Directors and corresponds to the Annual General Meeting, to which it is held accountable. In the case of listed companies and financial entities, the **external auditors should undertake external evaluations of the effectiveness and operational quality of the company's system of internal control** to detect possible weaknesses, given the risk that errors in the financial information compiled by the company may come up.

For the realization of the monitoring duties as for the own functions of account auditor, it is crucial that the **external auditor has a clear independence of the company**. This condition should be stated in the respective auditing report.

In the case of groups, the **external auditor should be the same for the entire group**, including "off-shore" branches.

Appreciation for the independence of the external auditor is a much discussed question that in practice may be broken down into four major points. In the case of listed companies and financial entities it should form part of their **policy for appointing the external auditor** and should be approved by the Board of Directors, which should include the following:

- A set of rules for choosing the auditor that take his/her professionalism and honorableness into account and stipulate that the Board of Directors may not propose to the Annual General Meeting the appointment of auditors who have been disqualified, suspended or subject to any other kind of sanction by a judge or regulatory authority in the corresponding country.
- In this point, the aim is to avoid absurd situations where an auditing firm that has been sanctioned by an administrative rule is forbidden to audit a certain types of companies but allowed to audit others due to the overlapping jurisdictions of different regulatory entities.
- The maximum term of the contract and the applicable extensions.
- Regulation of the provision of additional services.
- Regulation about the disclosure of remuneration.

The independence of the external auditors requires that a **maximum limit for the period of appointment** is established to avoid excessive linking between the auditing firms and/or their work teams, and the audited company. We estimate that this period should be between six to ten years. As a general principle, the auditing firms should be linked to the company by one or two year contracts, renewable subject to an evaluation of the performance and professional independence shown by the firm during the exercise of its functions and up to the maximum established limit. Within the maximum limit established, it is advisable that the **partners and work teams of the auditing firm rotate in the middle of the period, and that the auditing firm rotates at the end of the term**.

The terms we have just proposed intend to combine criteria for the renewal of the external auditors, with the need to dispoene of auditors with sufficient knowledge on the company's activities, so the necessary learning curve does not become a permanent burden for the effective provision of the auditing services.

Respecting the provision of additional services, we believe that as a general rule, **services other than those related to the account auditing itself should not be contracted with the external auditing firm.** The application of this rule should be extended to the persons or entities affiliated with the auditor; it should include the companies in his/her group, and the companies where there is a broad overlap between its partners and those of the auditing firm.

Nevertheless, there may be reasons justifying the procurement of additional services in a given moment, like a limited number of auditing firms or consultants in the country where the company engages in its activities. In those cases, it would be allowable to employ the auditor for other services, always provided they are of an exceptional nature and the Board of Directors agrees. The board should inform the General Meeting not only about the services the auditor or a person or entity linked to it provide to the company but also, about the **percentage of the cost of these additional services in the overall billing of the auditor**, which in our opinion should not exceed 40%.

Finally, in terms of disclosing the remuneration paid to the external auditor, we believe that **disclosing the total amount of the contract and the relative weight of the fees paid by the company in the income of the auditing firm** is a sound practice; that is, the percentage turnover the contract with company supposes to the auditing firm. In the policy for appointing the external auditor, we believe the ideal course is to exclude those firms in which the fees for the services provided to the company amount to more than two percent 2% of its total income.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
I 16. Undertaking an external audit of the effectiveness of the internal control system.	✓		✓
I 17. The same external auditor for the entire group.	✓	✓	✓
I 18. Policy for appointing the external auditor.	✓		✓
I 19. Maximum period and rotation of the appointment of the auditing firm.	✓	✓	✓
I 20. Hiring the auditing firms through one or two year contracts, renewable subject to evaluation.	✓	✓	✓
I 21. Rotation of the partners and work teams in the middle of the maximum period for the appointment of the auditing firm.	✓	✓	✓
I 22. Inadvisability of hiring the external auditing firm for services other than the account auditing.	✓	✓	✓
I 23. Limit and disclosure of the percentage of fees for additional services in the overall billing of the auditors.	✓		✓
I 24. Disclosure of the total amount of the contract and the relative weight of the fees paid by the company in the auditing firm's overall income.	✓		✓

V. Transparency and Financial and Non-Financial Information

In Corporate Governance, transparency has become a fundamental principle demanded both by the shareholders of a company and by the market as a whole, including not only stakeholders but other interested third parties. Transparency is understood as the act of revealing information about the company whose contents, format of presentation and timeliness have certain characteristics. It is the keystone on which the creation of the intangible asset associated with the building and transmission of trust, and where the good reputation of the company rests.

Its importance is strengthened by the fact that only when such information is revealed at a suitable level, the shareholders and interested third parties will be able to exert control over the company and, as in the case of the shareholders, exert their rights in an informed manner. In fact, transparency has evolved from a “**demand**” or “**right**” of the shareholders that companies voluntarily respect, beyond the minimum information required by commercial laws, into a “**duty**” of the companies and to the point where transparency has been subject to legal regulation in many countries.

Thus, different legislations have established certain obligatory minimums for revealing such information. They are found in a range of legal norms, but still leave a broad margin of discretion in the name of self-regulation. This margin is very broad in the case of companies not listed and much narrower for regulated companies like the listed ones and financial entities.

While it has been undertaken with different approaches and there has even been criticism of the idea of subjecting companies to an obligatory duty to reveal information, the evolution of transparency has traditionally been associated with listed companies and stock markets up to the present time, and that is the position taken by these Guidelines.

Transparency is a tool that should be used by all kinds of companies, regulated and non-regulated, in different degrees with the dual objective of:

1. Offering shareholders and investors as much information as possible so they can make a reasoned and rational judgment of a given company or an investment proposal; and
2. Exert an active control and lessen the possibility that the directors, administrators and members of the senior management of a company unduly take advantage of tangible benefits derived from the advantages of exclusive information, at the cost of or to the detriment of the shareholders.

V.I. Information Disclosure Policy (Guideline no. 39)

Listed companies and financial entities should issue a policy for disclosing information, which at least specifies the following:

- Which information should be revealed.
- How that information should be revealed.
- To whom the information should be revealed.
- Procedures to ensure its quality and thoroughness.

V.2. Financial Statements (Guideline no. 40)

The financial statements of a company should precisely reflect the most important aspects of its equity and economic-financial situation. This allows the current shareholders of the company to make sound judgments in order to make informed decisions. It also allows other operators in the markets who are interested in the future of the company, such as potential investors, rating agencies, creditors, communications media, etc. to obtain a reasonable knowledge of the company's performance.

The financial statements should be understood as the basic but not exclusive document to achieve this knowledge. The financial statements should contain at least the following information, to be able to understand a determined enterprise:

- An income statement.
- A balance sheet.
- A consolidated statement of changes in total equity.
- A statement of cash flows.
- A report of the external auditor on the financial statement and the auditor's notes.

The Board of Directors of listed companies and financial entities should **formulate and present audited financial statements to the Annual General Meeting, following the accounting principles** found in the International Standards on Financial Information (IFRS) and the International Accounting Standards (IAS), and in any case, those of a general nature applicable in the country where the company is headquartered.

In the case of corporate groups which are required to present consolidated financial statements, the results should be listed both in the consolidated statements and those of the parent company of the group. If the external auditor includes *exceptions* in the report, they will be explained to the shareholders. Even when the external auditor allows for *exceptions*, the board should maintain its own criterion, for example, for what are known as *uncertainties*. These should be adequately explained and publicly justified, with concrete information about the content and scope of the discrepancy.

Related-party transactions, including important transaction between companies in the same group ("intra-group" transactions), should be included in detail in the financial information of the company. It should also mention if **off-shore operations** have been carried out and when appropriate, communicate them at first instance as a relevant act.

In cases where the company's financial information is not subject to the IFRS, it will be appropriate to disclose the relations between the linked parties when there is a control, despite transactions have been carried out or not between such linked parties. This ensures that the users of the financial statement form an opinion about the effects of the existence of related parties has on the company.

Complementarily, the auditor's report should include the remuneration he/she receives in gross terms. Additionally, it should include the percentage that the services provided by the auditor to the company represent on the total billing of the auditor on a local level. In the cases where the external

auditor is contracted for services other than auditing, the report on Corporate Governance should include the proportion the amount received for these services represent compared to the auditing services done for the company.

In order to maintain the needed coherence and transparency, the financial information of intermediate periods and its relevant or important facts should be provided, following the same principles, criteria and professional practices used for the annual financial statements.

V.3. Information for the Markets (Guideline no. 41)

Within the framework of the policy for revealing information, the Board of Directors (or Auditing Committee) of listed companies and financial entities will adopt **the measures needed to guarantee that all the information on the company required by the legislation in force – financial and non-financial – is transmitted to the financial and capital markets**, as well as all the information investors and clients regard as relevant.

The **web sites** of the companies should be **user-friendly**, in such a way that access to information is simple. For this, the creation of five headings is recommended, whose minimum content should include:

1. **The company:** History, main facts, vision and values, business model, etc.
2. **Shareholders:** share price, dividends, capital, analysts coverage, relevant facts, press releases, financial information (annual report, management report, presentation of intermediate results, etc.), shareholder´s agenda, general assembly, shareholders contact, FAQs, etc.).
3. **Relations with investors:** results, reports (of results, operations, conferences, events, etc.), financial reports (annual report, management report, quarterly reports, report on risks management, information given to supervisory agencies, significant news, periodical public information, etc.), debt issuance, ratings, etc.
4. **Corporate Governance:** By-laws, Annual General Meeting and its regulations, composition of the Board of Directors and its regulations, board committees, Corporate Governance report, reports of the committees, rights to information, shareholders agreements, code of conduct, code of ethics, etc.
5. **Sustainability:** policies, interest groups, community, environment, etc.

The supporting tools to communicate different types of information may adopt different formats depending on each country´s tradition and current regulations. In general the documents should be user-friendly, in a PDF or PPT format that allows printing, downloading and sharing.

If the company decides to publish an annual report, there should be an electronic version as well as a printed one. We recommend that the information is structured in the following order:

- Financial statements drafted by the Board of Directors and presented to the Annual General Meeting

- The audit report, issued by the external auditor with its corresponding notes.
- Management report by the Chief Executive Officer.
- A Corporate Governance report from the Board of Directors.

We believe that financial entities should unavoidably publish a **report that explains the organization, methods and procedures of the control structure**. This allows for the collection of accurate and reliable financial and non-financial information, and safeguarding the assets of the company and the efficiency and security of its operations. The information on the control structure should be complemented by a **report on risk management**.

By virtue of the principle of informational transparency, the by-laws or other internal regulations should indicate that the transmitted information is correct, true and open to cross-comparison, and issued in a symmetrical, fair and timely manner.

V.4. Information about shareholders' agreements (Guideline no. 42)

Even if current local norms do not require companies to publish the agreements between shareholders, they are significant for the relation between the parties and the company, other shareholders or third parties. In the case of listed companies, the conclusion, renewal or amendment of a **pact or agreement among shareholders** should be immediately divulged to the company itself and the stock market. The pacts among shareholders usually aim to finalize, complete, or modify the legal and statutory rules on the internal relations governing the company.

These kinds of agreements can deal with matters such as the election of the members of the Board of Directors, the exercise of the right to vote in the assembly or the direction of the same on certain subjects or decisions which restrict the free transmission of shares, among others.

In the case of agreements made between shareholders of non listed companies, in all cases it is desirable that the society had knowledge about the agreement signed or at least, a summary of its contents.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
I25. Policy for disclosing information	✓		✓
I26. Information for the financial markets	✓		✓
I27. Report that explains the control structure	✓		✓
I28. Report on risk management	✓		✓
I29. Presentation of financial statements, in accordance with IFRS and IAS standards	✓		✓
I30. Related-party transactions as a relevant aspect	✓		✓
I31. Transparency of shareholders' agreements	✓		✓

V.5. Corporate Governance Annual Report (Guideline no. 43)

For listed companies and financial entities, a company's adoption and evaluation of the Guidelines should culminate in the **preparation of a Corporate Governance report**. The Board of Directors shall be responsible for its contents, and it will be subject to a report from the Auditing Committee. The report should be published annually in the annual report, if published, and the rest of the documents at the end of the financial year, but in the form of a separate document.

The publication of such information about Corporate Governance is based on the advantages that preparing and disclosing this report bring to the company in terms of transparency and credibility. Even more important, the Corporate Governance report is a useful tool that may be employed by the capital markets and its operators to evaluate the Corporate Governance of the company through the company's own explanation in the annual report.

Those companies that, due to their small size, do not prepare an annual report should include the information on Corporate Governance in their management report or a separate document. The importance of the annual report on Corporate Governance must be announced and when appropriate, incorporated on the company's website.

Consequently, the annual report on Corporate Governance is not a mere transcription of the norms on Corporate Governance found in the by-laws, internal regulations, and codes of good governance or other documents. It is not meant to describe the governance model of the company but to explain its functioning during the last financial year.

The report has an explanatory nature by which the company provides, on the one hand, objective information (for example, its capital structure or functions of the Board of Directors), and, on the other, information and precise facts that allow to understand how the different norms or practices of Corporate Governance affecting the company have or have not been complied. This includes the recommendations found in these Guidelines (for example on the number of meetings the Board of Directors hold and its degree of attendance).

Evidently, if the preparation and publication of this annual report is incorporated into the juridical framework of the countries in the region in the future, the public agency responsible for compliance with this norm must ensure that its contents are trustworthy and fulfill the minimum requirements, independent of the evaluation that the capital markets may do.

A. Information to be included in the Corporate Governance annual report

Among the items which should be included in the Corporate Governance report there are all those which are related to compliance with the measures set forth in the Guidelines, and particularly:

A.1 Ownership structure

- The capital and ownership structure of the company, to the extent it is known.
- The identity of the shareholders who, directly or indirectly, own a significant percentage of the total shares.

- Information about the shares owned by members of the Board of Directors, whether directly (in their names) or indirectly (through companies) and the voting rights they represent.
- The relations of a family, commercial, contractual or corporate nature existing between significant shareholders and the company, or the internal relations among the significant holders, to the extent that they are known to the company.
- Pacts among shareholders the company is aware of.
- The company's treasury stock.
- The existence of Board of Directors or Assembly agreements to neutralize take-overs.

A.2. Structure of the company's administration

- Composition of the Board of Directors and category of each member and of its internal committees.
- Powers delegated to the directors.
- Directors of the parent company who hold executive positions in subsidiary companies (the case of corporate groups).
- Policies approved by the Board of Directors.
- The process for appointing directors.
- The policy for compensating the Board of Directors.
- Compensation of the Board of Directors and members of the senior management.
- Guarantee or protection clauses in the cases of dismissal or changes of control which favor members of the senior management.
- Quorum of the Board of Directors.
- Attendance records of meetings of the Board of Directors and the committees.
- President (chairman) of the Board of Directors (functions and key issues).
- Secretary of the Board of Directors (functions and key concerns).
- Relations between the Board of Directors and the external auditor, financial analysts, investment banks and rating agencies.
- External consultants of the Board of Directors.
- Handling of the information to the Board of Directors.
- Functions of the board committees.

A.3. Related-party transactions

- Responsibilities of the Board of Directors for these types of operations and situations of conflict of interest.
- Details of the transactions between related parties, including intra-group ones.
- Conflicts of interest presented and the performance of the directors.
- Mechanisms to resolve conflicts of interest between companies of the same corporate group.

A.4. Risk Management Systems.

- Description of the risks policy.

- Materialization of risks during the financial year.

A.5. Annual General Meeting

- Differences in the functioning of the General Meeting when the minimum requirements of the country's company law apply and when those defined by the company's by-laws and other internal rules apply.
- Measures adopted to encourage the participation of shareholders.
- Information for the shareholders and communication with them.
- Limitations on attendance and voting.
- Details of attendance to the assembly.
- Details of the main agreements reached.

A.6. Degree of compliance with Corporate Governance recommendations

- "Comply or explain" model.

Recipients			
KEY RECOMMENDATIONS	Listed	Non Listed	Financial Entities
I32. Evaluation of Corporate Governance norms	✓	✓	✓
I33. Annual report on Corporate Governance	✓		✓

VI. Final Reflections on the Implementation of the Guidelines

The Guidelines provide a pragmatic and substantial view about a set of practices for Corporate Governance that companies should implement in order to strengthen their effective functioning, increase their sustainability and protect the rights of shareholders. For this reason, the Guidelines have been arranged into five key areas of Corporate Governance, related to three levels: ownership, administration and management. Each of these areas includes a group of Guidelines for Corporate Governance that in turn resulted in specific practices of Corporate Governance, which we refer to as Recommendations.

The development of these Guidelines, as they have been set forth here, may lead to the idea that the different areas are independent of each other, and even that the Guidelines and Recommendations specified for each of them are a scattered group of suggestions, without any inter-relation. However, that notion would be wrong, since it ignores that Corporate Governance should be understood as an integral matter and especially a coherent one. The practices of Corporate Governance that are in force in a given company must make up an integrated and effective set of rules similar to a *spider's web* that provides a series of reciprocal controls or checks and balances between the three levels of ownership, administration and management.

That is why the practices of Corporate Governance which are finally implemented in a given company in the five areas should constitute the governance model of the company. This model is understood as a set of principles and practices governing the organization and the functioning of the same. It is meant to provide the company with stability, efficiency, and above all, a clear assignation of roles and responsibility. The definition of a governance model rests on the assumption that the concrete practices of Corporate Governance detailed in the Guidelines should be adapted and implemented in the company, so that:

- They are consistent with each other.
- They point in the same direction.
- They make up a solid and integrated set of rules, that is, a logical, effective and coherent model for the needs of the company.

Contrarily, there is the risk of winding up with inefficient practices of Corporate Governance that may have a harmful impact on the efficient interactions necessary among the different levels of a company. Even worse, there is also the risk of not being able to form a group of reciprocal counterweights that truly lead to the minimization of risks in the governance of the company. In addition to this, any company interested in adopting and implementing the current Guidelines must carefully evaluate how it will start to apply them.

The purpose of this document is to encourage the companies of the region to implement the contents of the present Guidelines. However, we especially recommend the implementation of the Guidelines to be a gradual process, without brusque changes; it should not be forgotten that, in the last resort, the strengthening of Corporate Governance is not only a set of practices for governance

included in the documents on the internal corporate norms of a given company, but it also requires a cultural change, a different way of doing things at the heart of the company. For that reason, and basing ourselves on practical experience, we suggest that a process of implementing a good Corporate Governance in any company is based on the following principles of action:

- Ensure the integrality and coherence of the set of practices of Corporate Governance that make a governance model efficient and adapted to the needs of the company.
- Implement those practices of Corporate Governance whose value for the company is fully agreed on.
- Treat the process of implementation as a cultural change that requires time, since brusque changes may have negative effects on the company.
- Regard the governance model of the company as a dynamic one, so that it may be periodically adjusted and improved, in line with the changing circumstances of the company.

Having explained the above, we hope that these Guidelines will become a document widely known to the companies of the region, whether they are listed, not listed or financial entities, so that it contributes to the effective strengthening of their Corporate Governance, and in the end, of the region's corporate world as a whole.

We reiterate the advantages that the effective implementation of these Guidelines can have. They will help companies attract investments, improve their internal functioning, strengthen their sustainability, adequately protect the rights of shareholders, and in definitive, improve the management of their own governance risks.

Section III

REFERENCE
GUIDE TO THE
GUIDELINES

Prior Considerations

- The Guidelines found in this section are based in the considerations found in Section II, that go in depth into each one of the most critical aspects affecting current Corporate Governance.
- The interpretation of these guidelines should necessarily be done in line with what is set forth in the cited section. It also includes a second level of specific Recommendations that support the fundament of each Guideline that should be implemented through modifications of the by-laws and other internal regulations.
- Therefore, these Guidelines invite its recipients to reflect on the most important questions that arise from the governance of companies and the benefits deriving from the implementation of the Guidelines.
- These Guidelines are oriented towards three broad groups of companies: (i) **listed companies** subject to regulation and supervision where a wide base of shares are transacted in any economic sector, including financial services, and are quoted on an organized stock market; (ii) **non listed companies**, the category covering most of the companies of the region, many of which are family companies where a single family is the controlling shareholder; and (iii) **financial entities**, listed or non listed companies subject to regulation and supervision.
- The Guidelines compile concrete recommendations, whose orderly application will enable companies to comply with a number of demanding standards of Corporate Governance comparable to those recognized in the most developed economies. This way, investors, whether national or foreign, will not make the management of Corporate Governance a negative risk valuation factor that penalizes the analysis of a given investment when compared to other alternatives.
- The adoption of the Guidelines will require the reform of the company's by-laws and the approval of corporate norms in the form of internal regulations that establish concrete mechanisms of Corporate Governance.
- While initially the adoption of these Guidelines will be voluntary within the framework of the company's corporate autonomy, there is nothing to prevent some of its recommendations from being wholly or partly incorporated into the legal system of the countries of the region.
- It is understood that the assumption of these Guidelines are voluntary and the Annual General Meeting may set a reasonable term for its adoption; that does not exempt companies from strictly complying with them nor authorize companies to minimize the scope of the measures they contain.
- The Guidelines and their recommendation cover the following areas: (i) the Rights and Equitable Treatment of Shareholders; (ii) the Shareholders Meeting; (iii) the Board of Directors; (iv) the Control Structure; and, (v) Transparency and Financial and Non-Financial Information.

I. RIGHTS AND EQUITABLE TREATMENT OF SHAREHOLDERS

Guideline 1:

The company's acts should acknowledge the principle of equal treatment in its relationship with the shareholders, while this does not imply the acquisition of privileged information by one or several shareholders to the detriment of the rest of the shareholders who form the social capital.

Guideline 2:

The Board of Directors' proposals on certain corporate operations must necessarily be backed by the independent opinion of an external consultant with a recognized reputation for professional solvency, appointed by the Board of Directors and ideally, with the favorable vote of the independent external directors. These operations include capital injections, demergers, mergers and others that may negatively affect the shareholders' right to a non-dilution of its total stock.

Guideline 3:

All companies should implement permanent communication mechanisms with shareholders and investors, through which they may receive and ask for information, except when it is confidential or irrelevant. They may also ask questions of interest to the company or associated with their status as shareholders, other than the information provided at the Annual General Meeting. The answers to these questions shall be disclosed to the market, without privileging the soliciting shareholder with regard to the others. Listed companies and financial entities are required to have a corporate website.

Guideline 4:

Listed companies should not implement defense mechanisms that may be regarded as a protection against takeovers. In the case of non listed companies and mainly through a shareholders agreement, the "tag along" right of minority shareholders should be established for operations which imply a change in control of the company.

Guideline 5:

The by-laws shall include an arbitration clause that stipulates that any dispute between the shareholders and the company, between the shareholders and the Board of Directors, questioning agreements made by the General Meeting and the Board of Directors, or any demand that the directors fulfill their responsibilities, should be subjected to the arbitration of an independent local institution. If this happens in a foreign country, the institution deemed most convenient, except in case of express legal reserve to the courts.

II. THE SHAREHOLDERS MEETING

Guideline 6:

The by-laws must acknowledge that the Annual General Meeting is the supreme body. Especially, it should state its role in the governance of the company more dynamically by clearly defining its exclusive and non-delegable functions, including the appointment of external auditors, the approval

of the remuneration of the Board of Directors or the policy for treasury stock or the buying back of the company's own shares.

Guideline 7:

Listed companies and others with a wide base of shareholders should have regulations of binding nature for the Annual General Meeting, where sanctions exist for the violation of these regulations.

Guideline 8:

Through their by-laws, companies shall adjust the reality of their capital structure to the right of significant shareholders to call for an Extraordinary General Meeting; this meeting should take place within a reasonable lapse of time and fully respect the agenda proposed by its promoters.

Guideline 9:

The regulations of the meeting will set a time between the announcement and the holding of the Annual General Meeting, sufficient enough to announce the news in the media, including the electronic ones, that allow a maximum dissemination of the call, the minimum content of the announcement, as well as the obligation to detail the points of the agenda and the proposals to be agreed on; it should avoid the disclosure of vague information. The objective is to ensure a maximum attendance and the active participation of the greatest number of shareholders, and an understanding of all the proposals to be agreed on and in general the matters to be discussed at the meeting

Guideline 10:

Through the regulations of the meeting, companies should recognize the right of any shareholder to propose matters to be discussed on the agenda of the general shareholders meeting, provided there is reasonable notice in advance and agreement on a pre-established procedure.

Guideline 11:

Companies should establish means to facilitate the exercise of the right to information for all shareholders, prior to the holding of the Annual General Meeting and during the course of the meeting itself. This will facilitate their access to information and give them the possibility to request additional information or clarifications; always taking into account that the information must be complete, correct and transmitted to all shareholders on an equal basis and with sufficient time for them to analyze it.

Guideline 12:

The companies that should maintain a corporate website shall encourage and offer institutional investors the chance to make public their policy for participating in the Annual General Meeting, as well as the purpose of their vote on every of the proposals to be agreed on. In any case, the nature of the votes of the institutional shareholders shall be recorded, on an individual basis, in the minutes of the Annual General Meeting.

Guideline 13:

Companies shall guarantee the right of all shareholders to know the quorum needed to hold different meetings of the Annual General Meeting, the regime for the adoption of social agreements and,

the possible requirement of an enlarged quorum for those transactions that can significantly affect the rights of minority shareholders, as well as the conditions of and limitations on their attendance to the assembly.

Guideline 14:

The by-laws should stipulate the right of shareholders to call for the termination or application of sanctions for irresponsibility to members of the board directors at any time in the course of the assembly, even if it was not previously included on its agenda.

Guideline 15:

To facilitate and reduce the costs of the participation of non-resident shareholders to the assembly, companies shall promote before the public authorities the use of the electronic vote. To encourage the participation of shareholders in the general meeting, companies shall act in a neutral manner upon the grouping of shareholders.

Guideline 16:

When the General meeting is summoned, the Board of Directors shall provide the shareholders with a standard model for a letter of representation and reject the practice of delegating blank votes (without voting instructions) favoring the Board of Directors, its members and members of the senior management. The administrator who acts as a representative of a shareholder may not use the right to vote in cases where such decisions correspond to items on the agenda in where he/she could enter into a conflict of interest (termination, sanctions for irresponsibility, linked transactions). Administrators who are also shareholders may employ their own voting rights on any subject, except those of a personal character where they may enter into a conflict of interest.

Guideline 17:

The Chief Executive Officer (CEO) shall present his/her management report to the shareholders. Directors and, especially, the presidents of committees shall be encouraged to attend the Annual General Meeting, along with all the executives or external consultants whose presence and explanations about the subjects to be covered will make it easier for shareholders to understand.

III. THE BOARD OF DIRECTORS

Guideline 18:

Regardless of their type, companies should have a Board of Directors with a number of directors that is sufficient for the adequate performance of its functions and the formation of the necessary committees.

Guideline 19:

Among the general functions of strategic planning, supervision of specific matters, control of day to day management, governance and administration, the by-laws or regulations of the Board of Directors should stipulate the specific functions that may not be delegated.

Guideline 20:

Companies should have regulations for the Board of Directors of binding nature for its members, and sanctions for their violation.

Guideline 21:

The by-laws shall determine the minimum and maximum number of members allowed on the board of directors. Each general meeting will determine the exact number of directors to be elected. This will ensure an effective administration and governance of the company at all times, and also the active participation of directors proposed by significant shareholders (external patrimonial directors). The need to complete a quorum shall not justify doubling the number of directors through the appointment of deputy directors who should not exist.

Guideline 22:

On the assumption that the board of directors is a unitary and collegiate body that supposes a single regime of responsibility that is the same for all of the directors, it is important to know “**who is who**” among its members, as well as the source of their appointment. The board of directors may be constituted by internal and external directors who in turn, may be independent or patrimonial ones. As far as possible, the appointment of the directors will try to reflect the shareholding structure of the company. When internal directors exist, the practice by which the external directors represent a wide majority shall be respected.

Guideline 23:

The board in exercise can play a key role in the processes of determining its needs as well as for the search, evaluation and candidates' nomination. These processes should be governed by a formal and transparent procedure, undertaken with professional criteria. The details of these should be included in the regulations of the board, with the final responsibility of the Nominations and Remuneration Committee. Evidently, if the shareholders wish, they could have the right to nominate candidates at the Annual General Meeting. In addition to helping the Board of Directors to be more effective, the staggered election of directors may facilitate the processes that take place prior to the election of its members. In countries where the law allows it, the system for electing directors should be the cumulative vote.

Guideline 24:

The company may only designate, as independent external directors, those who fulfill the requisites of professional experience, honorableness, economic independence and an absolute absence of links with the company and its shareholders, administrators or personnel. External directors shall make their independent nature known to the public through a public declaration of independence signed both by the designated director and the Board of Directors binding on the director's future actions.

Guideline 25:

The by-laws should establish the causes for the termination of directors as well as their obligation to resign if they fail to comply with the conditions of their appointment or if they could damage the prestige or good name of the company.

Guideline 26:

The by-laws shall set forth the scope of the duties of diligence, loyalty, non-competition, secrecy and non-use of the company's assets, as well as their rights to information, the help of experts, training and compensation.

Guideline 27:

The by-laws should expressly stipulate the handling of situations of conflict of interest, both personal and due to specific activities when they occur. The Board of Directors should approve the corresponding policies in the case of personal interests. These policies should state that the affected directors are obliged to absent themselves or restrict their role in discussions and voting in these situations. They should also state the regulations for the evaluation, approval and disclosure procedures when dealing with related-party transactions. The directors should present a general declaration of links, including all of the direct or indirect relations they have among themselves and with the company, its shareholders, senior management, suppliers, clients or any other groups of interest from which situations of conflicts of interest or influence their opinions or votes may arise.

Guideline 28:

The directors should be sufficiently compensated. The Annual General Meeting, following a proposal by the Board of Directors, shall approve the payment policy for the board. As a general norm, it should set the maximum limits of payment for each component and may include mixed systems, part of the payment linked to variable components measured by the performance of the company. At the end of each financial year and before the Annual General Meeting that must approve the accounts, the Nominations and Remuneration Committee will fix the specific and definitive amount of remuneration for each director. The regulations of the Board of Directors will establish the requisites of transparency required for the remuneration of the directors, disclosed ideally in the annual report on Corporate Governance.

Guideline 29:

The internal organization of the Board of Directors, and the correctness of the appointments to its positions, should enable it to act as an effective counterweight to the senior management. They may also act as a link to the shareholders, so that the shareholders do not become hostages of the board.

Guideline 30:

In normal conditions, companies should try to separate the administration or governance of the day to day management of the company through a correct delegation of functions to the senior management. This way the Board of Directors does not interfere in day to day affairs and can focus its actions on the general functions pertaining to it. The pertinence or exclusion of the CEO on the Board of Directors, his functions, the evaluation of his performance and the payment system are crucial variables to take into account when ensuring that the separation between administration and day to day management adds value to the company, and does not entail inefficiency or additional risks.

Guideline 31:

In addition to the composition and functions of the Board of Directors, an adequate planning of its dynamics under the leadership of its president (chairman) is seen as a crucial element that should positively contribute to its efficiency. Every year, the number and calendar of its ordinary meetings should allow it to optimize a work plan related to the functions it is commended with. When the company counts with experienced and diligent directors, the sufficiency and quality of the information they receive will have a decisive influence on the development of their meetings. An annual evaluation of the board will enable the company to draw conclusions about its work as a collegiate body, as well as of its members on an individual basis.

Guideline 32:

The Board of Directors will establish internal specialized committees for support and study, made up of external directors with the capacity to present proposals to the board. In every kind of regulated company, the exercise of the functions associated with the control structure should draw on the support of an Auditing Committee, or its equivalent. In the case of financial entities, the creation of a Risks Committee should be imperative due to the nature of their operations.

IV. CONTROL STRUCTURE**Guideline 33:**

The Board of Directors has the ultimate responsibility of ensuring that the control environment promotes a true risk culture within the organization, defining the corresponding roles and responsibilities for, from those most closely associated with specific processes, to those deriving from the definition of the company's strategy.

Guideline 34:

The board of directors should approve an integral policy for risk management. Within the framework of that policy, it should periodically examine and supervise the actual exposure of the company to the identified risks. The management of these risks will depend on the senior management. For certain types of companies, conforming highly skilled managerial teams seems necessary for handling risks.

Guideline 35:

The Board of Directors is responsible for the existence and supervision of the company's system of internal control. This system must be based on the principle of self-control, understood as the capacity of people who participate in the processes to consider such control an inherent part of their responsibilities.

Guideline 36:

The culture, philosophy and risks policy should be disclosed in a descending and transversal manner, so it permeates the whole organization. This will delimit acceptable and unacceptable

conducts and will facilitate denouncements by employees of conducts that may go against the company's control culture.

Guideline 37:

The company should guarantee the autonomy and independence of the internal auditing teams in the exercise of their duties of monitoring and evaluating the effectiveness of the company's control structure. Towards that end, the appointment and termination of the person responsible for internal auditing will correspond to the Board of Directors, among other practices.

Guideline 38:

External auditing is another pillar necessary to monitor effectively the company's control structure. This way its independence would be guaranteed to the shareholders through the formalization of a set of practices related to the contracting of the external auditing firm, ranging from the rotation of firms and their partners to limitations on the provision of services other than auditing.

V. TRANSPARENCY AND FINANCIAL AND NON-FINANCIAL INFORMATION

Guideline 39:

Transparency should be regarded not only as a right of the shareholders, but also as a need and even a duty of companies. Shareholders should comply with transparency in a harmonious way through the publication of a policy for disclosing information approved by the Board of Directors.

Guideline 40:

To understand the company's situation better, the public financial statements should not be limited to an income statement or balance sheet; it must include the set of reports which make it up, in addition to complying with local accounting norms. Listed companies and financial entities should at least voluntarily adopt, as far as possible, the IFRS/IAS standards for the preparation of their financial statements, even if it is not required in their country of domicile.

Guideline 41:

Within the framework of the disclosure policy, the Board of Directors shall promote the practice of supplying information to the operators of the financial and capital markets, as well as the community in general, without placing the integrity of the company at risk. The disclosure should go beyond the minimum legal limits, through the issuance of reports that complement the obligatory ones and insist on the due certification of the financial statements. The company shall safeguard the accuracy, truthfulness and comprehensibility of the information by transmitting it in a symmetrical, equitable and timely manner. For that reason, the company's corporate web site must be structured in a user-friendly way.

Guideline 42:

As a general principle, agreements between the shareholders of listed companies must be disclosed to the market. Only the corresponding supervisory body will be able to authorize that such information must be reserved for a given maximum period.

Guideline 43:

The Board of Directors should approve and publish an annual report on Corporate Governance that includes the extent to which the company has complied with these Guidelines, as well as detailed corporate information and information about related parties and conflicts of interest.

Section IV
ANNEXES
OF THE
GUIDELINES

Annex I - Corporate Governance for Groups

The content of the Guidelines for a Latin American Code of Corporate Governance, including every Guideline and recommendation that compose it, are directly applicable to individual companies, and distinguish between listed and non listed companies, and financial entities. However, the corporate reality of the region shows the gradual formation of important corporate groups, both national and regional, that have a strong economic impact and a growing and significant influence.

Meanwhile, the financial markets in general have gone through a process of substantial concentration that has led to the creation of financial conglomerates (business groups for financial services, usually linked with banking, insurance and securities), many of them operating beyond their national frontiers, which turns them into indispensable actors in regional financial markets. Today, it would be not possible to understand the business environment in the region without considering these corporate organizations. They confront challenges of their own in terms of Corporate Governance, given the apparent contrast between their economic unity; derived from the search for a common objective as a group, and their juridical plurality, since they are made up of different independent companies.

From an academic conception, the groups are private responses to the need to organize and run businesses of various kinds. The groups serve as a way to organize the company's juridical and economic aspects of the business activity in the different ventures, whether they are financial or entrepreneurial.

The main common feature of corporate groups and financial conglomerates, by which they may be defined, is that they are interlinked through the existence of a judicially independent parent or holding companies. The parent company owns shares directly or indirectly in all or part of the capital of each of the subordinate companies and exerts a common control or effective influence on the same company.

Consequently, there are two joint and necessary conditions to consider, when determining the existence of a business group or financial conglomerate:

- Share ownership; and additionally,
- An effective influence or common control exerted by the parent or controlling company over its branch companies, understood as the direction exerted by a parent or controlling company over the companies that integrate the group to attain a common objective.

It is in the exercise of the control of the parent or controlling company where the possibility of seeking efficiency through the creation of synergies lies. This not only justifies the existence of the group itself but also, helps it achieve its objectives. From the perspective of Corporate Governance, this means that it must face challenges inherent in:

- On one side, the creation of synergies through the continuous quest for efficiency derived from the definition of a common objective through the formulation of a group strategy; the issuance of guidelines and policies with a group scope; the design of mechanisms for its canalization through the different companies of the group; and, the implementation of channels

of communication and flows of information, all of which allow for the coordination of the activities and operations of the group.

- On the other, the respect that should be paid to the reasonable autonomy of the companies that integrate the group, given their status as legally independent companies - recognized and protected by the legal system.

In the face of this challenge, it must be considered that the issuing policies and guidelines that apply to groups as a whole, as a way to attain a common objective (that of the group), may clash with the autonomy the law grants to each company, regardless they belong to the group or not, and their individual interests.

Our position is that by forming part of a group from which they benefit (and from which they obtain common services, financial and non-financial resources from the group, and other advantages), the subordinate companies should accept that there actually exists **an interest pertaining to the group they belong to and that it should be regarded as the primary interest all the companies of the group should pursue and defend.**

And why do we say that the interest of the subordinate companies should be regarded as subject to the interest of the group which dominates them? Because the subordinate companies do not have the autonomy to exert their own will without interferences. In terms of social capital, they are subordinate to the parent company, which also exerts a notable influence over them. This excludes the traditional idea of the individual social interest of the companies belonging to a group, to consider the self-interests of the group as the key to defend. This concept should be used to resolve the possible conflicts of interest that arise between companies in the group.

In this sense, Corporate Governance turns into a crucial tool that allows for both the definition and the defense of the interest of the group itself, as the creation of synergies. This not only justifies but also, maximizes the value of the group, maintaining the necessary respect to the autonomy of the companies which make it up. In particular, in terms financial conglomerates, the role of Corporate Governance is even more important given the following variables:

- The complexity of the financial and non-financial risks to which they are exposed.
- The dynamism of the sector.
- The high ratios of leverage with which they operate.
- The need to protect depositors.
- Systemic risk, including trans-frontier ones.

These variables, along with the events occurred worldwide at the beginning of the global financial crisis in 2008, have drawn a growing attention to the agencies that supervise Corporate Governance in banking and financial entities subject to supervision. It has also drawn attention to the financial conglomerates themselves, given their growing importance and evident complexity.

A good proof of this is the profound advances in the field that have come about in recent years. They reinforce on local regulations in most countries and from the perspective of the supervisory bodies,

with the publication of the *Principles for the Improvement of Corporate Governance (Principios para la Mejora del Gobierno Corporativo)* in October 2010, and the *Principles for the Supervision of Financial Conglomerates (Principios para la Supervisión de Conglomerados Financieros)* in September 2012, both in charge of the Joint Forum of the Basel Committee on Payment and Settlement Systems.

All of the above justifies the principle that the Guidelines should not ignore the treatment that from the perspective of Corporate Governance should correspond to both business groups and financial conglomerates. It necessarily requires specific practices of governance that are not strictly the same as those stipulated for individual companies.

From the standpoint of Corporate Governance, the key to this lies in the existence of a **governance model for groups**, whether they are business or financial groups. This model is understood as the set of principles and practices of Corporate Governance that govern the organization and the functioning of the group as a whole and are meant to provide it with stability, efficiency and above all, clarity about the assignment of roles and responsibilities.

The definition of a governance model presupposes that the concrete practices of Corporate Governance detailed in the Guidelines should be adapted to, and implemented on the different levels of the group, especially on the level of the parent company and subordinates ones, so that they are:

- Compatible among them.
- Point in the same direction.
- Form a solid and integrated set, that is, a model that is logical, effective and coherent.

In the present Annex I on the Corporate Governance of groups, the following key areas are discussed:

1. The structure of the group.
2. The treatment of the Board of Directors.
3. The consolidated treatment of the control structure.
4. Transparency and disclosure of information.

I. Definition of a transparent organizational structure that allows the assignment of clear lines of responsibility.

Both, business groups and financial conglomerates, show a strong heterogeneity in their organizational structures, given their different characteristics, activities, needs for coordination and even ownership structures in the subordinate companies. These and other factors have led to a profound development of the discipline of organizational design, given the profound strategic and operational implications the definition of a suitable organizational structure has for the efficiency of any group.

In particular, from the perspective of Corporate Governance, the organizational structure should allow the parent company to exert an effective supervision of the group of subordinate companies. It should also be suitable for the nature, scale and the complexity of the group and its risks, both joint and of the individual companies that make up the group.

In addition, the organizational structure should allow for the assignation of clear lines of responsibility within the group, in a way that facilitates the control and effective supervision of the group as a whole and the individual companies belonging to it.

With respect to financial conglomerates in particular, it is especially convenient that each subordinate company have an exclusive social purpose, that is, that each company that integrates the conglomerate has a single activity of a financial nature (banking, insurance, brokerage, funds management, remittances or others). This facilitates an effective control and supervision by the parent company and the regulatory agencies.

Given the special nature of financial conglomerates and the risks to which they are exposed, it is not suitable to include in them other companies that carry out activities other than the provision of financial services.

Finally, all the companies integrating a financial conglomerate should be subject to supervision by the corresponding body of control, including the parent company, regardless it is operational (the case of a bank that acts as the parent company of a conglomerate) or not (the case of a holding company).

Guideline for Groups I: The existence of a public organizational structure that is clear and transparent, and allows for the assignation of clear lines of responsibility facilitates the strategic guidance, supervision, control and effective administration of the group.

Recommendations on Guideline for Groups I:

In specific terms, the organizational structure of the group should determine the following aspects:

- 1.1 The main branch and subordinate companies of the group, the places where they operate and their social domicile.
- 1.2 The way in which the group is administered and controlled at the highest level.
- 1.3 The main lines of responsibility within the group.
- 1.4 The significant interactions among the different lines of management in the group.
- 1.5 The mechanisms for coordinating the group and the channels of communication within the group and flow of information.
- 1.6 The corporate, financial, commercial and other important relations among the different companies of the group.
- 1.7 In the case of financial conglomerates, the establishment of subordinate companies with an exclusive social purpose.

2. Treatment of the Board of Directors

Just as the Guidelines indicate, the Board of Directors is the body of governance in any company, responsible for its representation, governance and supervision, as well as any activities necessary to attain its social purpose.

The case of corporate groups or financial conglomerates is not an exception to the above, with the particularity that a distinction should be made between the Board of Directors of the parent company and those of the subordinate companies, acknowledging a **differentiated treatment of the Boards of Directors**.

While the Board of Directors of the parent company is responsible for carrying out a set of functions that apply to the group as a whole, which implies a greater intensity and dedication, the Boards of Directors of the subordinate companies must answer to a double level:

- that of its own subordinate company; and,
- that of the parent company with regard to the activities of the subordinate company within the group.

Therefore, differences could exist between the Board of Directors of the parent company and that of a subordinate company, due to the different scopes of their responsibilities. Consequently, it may lead to the establishment of a different composition, organization, assignation of functions and dynamic.

The above does not imply that the set of Guidelines and Recommendations that the *Guidelines* propose for the Board of Directors are not applicable to the companies that are part of a group or conglomerate. Rather, they are fully applicable but adapted to:

- The particular reality and complexity of the group and the companies that make it up.
- The real influence which the parent company exerts over the subordinate ones; and,
- The different importance of the subordinate companies, relative to the group as a whole.

Having established the above, in the present annex we explain our view of some specific matters we regard as especially important and have to do with the different treatment of the Boards of Directors of the parent company and of the subordinate ones:

- a. The assignation of functions.
- b. The composition of the Board of Directors.
- c. Organizational practices and functioning of the Board of Directors.
- d. The Board of Directors committees.

a. Assignation of functions

Guidelines for Group 2: there should be a differential treatment of functions formally assigned and exercised in practice by the Board of Directors of the parent company and those of the subordinate companies.

Recommendations on Guidelines for Group 2:

At the level of the Board of Directors of the parent company:

In specific terms, the differential treatment of the functions requires that the by-laws or regulations of the Board of Directors of the parent company assign a set of functions with a group-wide scope that should be exerted in practice.

As the Guidelines recognize, these functions are linked with the **strategic guidance** of the group, the **supervision** of the group, the **control** of the line of the group's senior management and the **execution** of certain administrative acts with a group-wide scope.

For that reason, the board of the directors of the parent company should:

- 2.1. Oversee the existence of an adequate governance model in the entire group, for which it should provide common policies and guidelines, as well as ensure that the practices of Corporate Governance of the group are consistent internally.
- 2.2 Define and examine the guidance strategy of the group and monitor the performance of the group in terms of the strategy and defined objectives.
- 2.3 Review and approve the group's governance structure, as stipulated in the previous Guideline I.
- 2.4 Safeguard the existence of adequate control structure at the group level.
- 2.5 Be aware and effectively undertake a follow-up of the risks to which the group is exposed on a consolidated level.
- 2.6 Directly control the management line of the parent company – if it exists – or indirectly control the management line of the subordinate companies through their Boards of Directors.
- 2.7 Approve group policies and guidelines, normally linked to a set of key aspects, among which the procedures for appointing the Boards of Directors, remuneration policies for the Board of Directors and senior management, or transparency and the divulgation of information figure.

At the level of the Board of Directors of the subordinate companies:

The differential treatment of functions requires that the by-laws or regulations for the Board of Directors of the subordinate companies formally assign a set of functions to the board of the subordinate company. In practice, it should exercise a set of functions within the context of its membership to the group.

As a general rule, the Board of Directors of the subordinate companies should usually:

- 2.8 Provide strategic information to the parent company.
- 2.9 Monitor the performance of the subordinate company with respect to its strategy and objectives.
- 2.10 Implement the group's policies and guidelines in coordination with the senior management as long as they do not jeopardize the viability of the subordinate company.

- 2.11 Supervise specific matters in accordance with the existing guidelines and policies of the group, such as the control structure, remuneration policies or the disclosure of information.
- 2.12 Control the senior management of the subordinate company and safeguard the qualifications and skills it has for the position exercised.
- 2.13 Render account to the parent company.

b. Composition of the Board of Directors

Guidelines for Groups 3: The Boards of Directors of the companies of a group must be integrated by a number of members with a combination of profiles that allow for the adequate function in the practice of the assigned functions.

Recommendations on Guidelines for Groups 3:

At the level of the Board of Directors of the parent company.

The correct exercise of the functions assigned to the Board of Directors of the parent company under the norms depends on the board having a sufficient number of members, with adequate profiles, among other factors, to support an effective exercise of the assigned functions.

Evidently, determining the right size of the board and defining the necessary profiles will fundamentally depend on the size and complexity of the group and the strategy defined in each case. However, one may lay down criteria that in a general way should influence the composition of the board of the parent company, which should:

- 3.1 Be integrated by a number of people sufficiently qualified to perform the functions assigned to them. This requires their ability to analyze and understand in depth the matters that are within the competence of the board.
As a general rule, this number should vary between seven and eleven members.
- 3.2 Be composed of a set of profiles related to the strategy defined by the group, which includes appropriate experience, skills, personal and professional talents and sufficient time to devote themselves to the performance of their function.
- 3.3 Establish rotation mechanisms for the members, in order to strengthen the suitability of the profiles to the group's strategy.
- 3.4 Arrange training and preparation programs on matters of interest for the exercise of the functions of the Board of Directors that will allow its members to improve their skills and capacities.

At the level of the Board of Directors of the subordinate companies:

The Board of Directors of the subordinate companies within a group will logically be influenced both by the relative importance of the subordinate company in the context of the group and the

presence or not of shareholders external to the group. They will also be influenced by the Board of Directors of the parent company.

In particular, the board of the directors of the subordinate companies should:

- 3.5 Be integrated by a number of members sufficient to exercise their functions, which should normally be less than in the case of the Board of Directors of companies that do not belong to a group, given the limited exercise of their functions. As a general rule, this number should range between three and seven members.
- 3.6 Be integrated by a set of profiles with the appropriate experience, skills, personal and professional talents and sufficient time to devote themselves to the performance of their functions as members of the Board of Directors.
- 3.7 These criteria should be especially evaluated by the Board of Directors of the parent company when it comes to proposing candidates to join the Board of Directors of the parent company.
- 3.8 It is acceptable that the positions on the board of the subordinate company include people who follow the line management of the subordinate company or group, but they should be a minority.

c. Organization and functioning practices

Guideline for Groups 4: The practices for the organization and functioning of the Boards of Directors of the companies that make up the group, both of the parent and subordinate companies, must be adapted to the characteristic culture, reality and needs both of the group and, in the case of the subordinate companies, their complexity and relative importance within the group.

Recommendations on Guideline for Groups 4:

At the level of the Board of Directors of the parent company

Regarding the Board of Directors, the Guidelines underline that it is important from the perspective of Corporate Governance that this body should define, provide details and formalize its practices of organization and functioning. This way the Guidelines will directly strengthen the efficient exercise of the board's functions.

In the context of a group, whether it is a business group or a financial conglomerate, this practice is important given the complexity of these kinds of organizations. The Board of Directors of the parent company is very important for the governance practices of the group as it can influence the board of the subordinate companies.

Thus, the treatment of this practice proposed in the Guidelines is fully applicable to the Board of Directors of the parent company, which in particular should:

- 4.1 Define and periodically revise its **practices of organization and functioning** that should be **formalized** in the internal norms.
- 4.2 Have a **suitable structure** in terms of the size, frequency and duration of its sessions, and the use of committees, which should be consistent with the complexity of the group, thus contributing to its efficient performance.
- 4.3 **Evaluate its functioning** as a body and of its members individually, using an **external firm** to achieve more efficiency in its performance.

At the level of the Board of Directors of the subordinate companies:

The practices of the organization and functioning of the Board of Directors of a subordinate company should be strongly influenced by its relative importance in the group, and in particular, the functions assigned to it.

Consequently, the Board of Directors of the subordinate companies should:

- 4.4 Define and periodically revise their practices of organization and functioning. They should be formalized in their internal norms and particularly, ensure they are consistent with their functions, its relative importance in the group and the influence of the Board of Directors of the parent company.

d. Board of Directors Committees

Guidelines for Groups 5: Except when it is required by the applicable legal framework or regulator, the Boards of Directors of the subordinate companies may not establish specific committees for the treatment of certain matters and these should be assumed by specific committees of a group-wide scope.

Recommendations on Guideline for Groups 5:

At the level of the Board of Directors of the parent company

The parent company of a group usually establishes specific board committees with a group-wide scope to handle certain specific matters. With this, it promotes a common treatment for a group of aspects, to strengthen the group's consolidated management of these matters and ensure their homogenous treatment.

Except when it is required by the applicable local norms, framework or regulator, it is unnecessary to replicate committees on the subordinate company level. This practice ensures the creation of synergies and of a consolidated supervision on a group level. Therefore, in terms of committees, the Board of Directors of the parent company should:

- 5.1. Except in exceptional cases, **avoid creating an excessive number of committees** with a group-wide scope within the Board of Directors, always assessing its objective and fit into the structure of the group.
As a general rule, the committees that should be constituted in a group are **auditing, nominations and remunerations**, and in the specific case of financial conglomerates, a **Risks Committee**.
- 5.2. The composition of the committees should be based on the suitability of their members in terms of their profile and the purpose of the committee itself.
- 5.3. When establishing committees in the board with a group-wide scope, it should be clear if these have **functions delegated** by the Board of Directors itself, or are only focused on **support and analysis functions** to the directory, relevant to the specific purpose of the committee.
- 5.4. As the Guidelines indicate, oversee that each committee has its **own regulations**. Norms should be established to oversee its organization and functioning, and in all cases, its objective, the scope of its activities, its functions and rules of functioning.
- 5.5. Finally, assess whether it is convenient or not to establish **equivalent committees** on the level of the subordinate company. Except when it is specifically required by the legal framework or regulator, the board committees with a group-wide scope should exercise these functions.

At the level of the Board of Directors of the subordinate companies:

Once it is deemed convenient to establish committees with a group-wide scope for the treatment of certain matters, it may also be suitable to establish specific board committees for a subordinate company. This could happen due to the applicable legal framework or regulator, relative importance of the subordinate company or other operational and strategic factors. That is why the Boards of Directors of the subordinate companies should in terms of committees:

- 5.6. Establish **specialized committees, always provided that it makes sense for them** to exercise their functions in practice, examine the work of equivalent committees with a group-wide scope, and ensure that their members are suitable for the functions of the committee.
In the case of financial conglomerates, it frequently occurs that the legal framework and regulator demand the establishment of Auditing and Risks Committees on the individual entity, independent of the existence or not of committees for these matters with a group-wide scope.
- 5.7. Oversee that each board committee on the subordinate company level has **internal regulations** with rules for its organization and functioning.
- 5.8. In particular to the Auditing Committee, verify that it is exclusively made up of members of the board who do not also have management functions, either in the subordinate company itself or on a group level.

3. Treatment of the control structure

The Guidelines devote a special area to the control structure that highlights the importance of its five components, in line with the treatment found in COSO I and COSO II:

- **Control Environment:** understood as the responsibilities, policies and processes defined for control. It is the main component of the control structure, since it serves as the basis for the rest.
- **Risks administration:** understood as the strategies and factors responsible for the identification and management of risks in the organization.
- **Control activities:** understood as the policies and procedures that help the management line ensure the responses to risks are executed in a timely and appropriate manner.
- **Information and communication:** understood as the process of communication in the entire organization, needed for the functioning of all of the control structure.
- **Monitoring:** understood as the process of evaluation to ensure the effective functioning of all of the control structure.

Once again, the contents of this area are applicable to business groups and especially financial conglomerates, for which it is a matter of maximum importance.

From a group perspective, the control structure should be an area of special significance; it allows for the consolidated supervision on a group level, for the fulfillment of the strategic objectives, controlling and managing the risks posed for the group as a whole.

Given the complexity of this matter, from the perspective of Corporate Governance, it is not a question of designing a specific and detailed model of the control structure. Every group should develop its own model, in accordance with its complexity and needs, while ensuring its design is based on the best international practices in the field, particularly COSO I, COSO II and the future COSO III.

Guideline for Groups 6: The existence of a control structure should be based on the best practices, with a formal and consolidated range, covering all of the levels of the group. It should also establish different responsibilities by defining clear lines of report that allow for a consolidated view of the risks to which the company is exposed and taking the appropriate measures of control.

Recommendations on Guideline for Groups 6:

The group's control structure should specifically:

- 6.1. Establish the responsibility of the Board of Directors of the parent company to oversee that there is an **adequate control structure** adjusted and adapted to the group's reality and complexity, based on the best practices in the field (COSO I, COSO II and COSO III).

- 6.2. Approve a **control policy and risk administration policy** with a group-wide scope, to be implemented in the different subordinate companies, allowing for a consolidated vision of both matters.
- 6.3 Assign the management of the control structure to those with **the highest responsibilities in the group**, whose positions are of maximum importance in the management line and with clear reporting lines.
- 6.4 **Involve the entire organization** with different levels of responsibilities in line with the control structure, in order to promote its effective functioning.
- 6.5. Assign a **group of functions related to the control structure to the board of the subordinate companies**. This way they are responsible for implementing the control and risks management policies for the groups in the subordinate company, as well as adjusting the subordinate company's control structure to the published guidelines.

4. Transparency and disclosure of information.

Information is an asset of enormous value. Regardless of whether it is mandatory or voluntary, information is crucial when a third party wishes to form a well-rounded opinion about the reality of a group and the activity of its administrators, and analyze its risk level. Nevertheless, transparency has often been regarded as an end in itself, when in reality it has an instrumental character.

Particularly in groups, information is an essential aspect that enables people to attain a consolidated vision of the group. It is not exclusively limited to a compilation of information about the individual companies integrating the group, but also includes transversal information, integral to the group as a whole. It thus, provides a faithful picture of it.

The Guidelines set aside a specific area for a whole set of specific guidelines and recommendations about transparency and the disclosure of information, which are fully applicable to groups and may be adapted to the reality and complexity of any group.

Guideline for Groups 7: The disclosure of integral and transversal information about the group per se to third parties enables external third parties to form a reasoned opinion about the reality, organization, complexity, size and governance model of the group.

Recommendations on Guideline for Groups 7:

In specific terms, each group should publicly disclose information to interested third parties as a sound practice. In the absence of third parties, it should disclose exclusively to its shareholders and investors, information which is sufficient for them to make a well-founded judgment of the reality, complexity and functioning of the group.

Thus, in terms of transparency and disclosure of information, a group should:

- 7.1. Develop a policy for **transparency and disclosure of information**, establishing the main criteria for disclosing information and the people responsible. It will be approved by the Board of Directors of the parent company, with a group-wide scope that should be channeled towards the different companies in the group.
- 7.2. Develop and publish a **corporate web site for the group**, including:
 - A brief summary of the group, with a description of the group and its main business ventures.
 - An organizational chart of the group.
 - Audited financial statements and other relevant financial information about the group that may affect the local financial entity.
 - A report on the governance of the group and its annual report.
 - A description of the group's governance model and changes made to it.
 - Related intra-group transactions that have a significant effect on specific subordinate companies.
 - The names and a summary of the CV and profile of the board members of the parent company and of the key positions on the management level and changes that could occur.
- 7.3. In the context of the **subordinate companies'** membership to the group, the following should be disclosed:
 - The Corporate Governance structure of the subordinate company and the way in which it is included in the governance model of the group.
 - Clear and precise financial and non-financial information, presented in a straightforward and comprehensible way for the addressed public.
 - The precise implications for Corporate Governance of their membership to the group.

Conclusions

The definition of a governance model for a group, whether it is a business group or a financial conglomerate, is a crucial aspect at the time of a possible creation of synergies of a corporate type. These synergies maximize value as well as a coordinated and efficient conduct of the different companies which make up a group.

For that reason, it would not make sense to implement the entire contents of the Guidelines in each company of the group in an isolated manner. Instead, it would be better that each company is aware of its membership to a group and consequently, define and implement a governance model for the group as a whole. Based on the Guidelines and their recommendations, the governance model may be adapted to the reality and complexity of its components.

Towards that end, the present annex includes an analysis of three main areas that should be covered by the group's governance model. It also sets forth some specific guidelines for the group, each accompanied by its own recommendations.

The challenge for any group aiming to strengthen its Corporate Governance is to employ the principles set forth in this annex, complemented by the detailed treatment of practices described in the Guidelines. This will allow them to design and structure its own governance model and ensure it is fully adapted to its special characteristics. This way they may obtain the greatest synergies and guarantee its efficient and harmonious functioning.

Annex II - The responsibility of financial entities in the promotion of Corporate Governance

The Guidelines for a Latin American Code of Corporate Governance (GLACCG) provide a set of guidelines and recommendations aimed at companies (as well as business groups or financial conglomerates in its Annex I) that voluntarily decide to strengthen their practices of Corporate Governance.

With it, the idea is that companies – and business groups or financial conglomerates – will have a document considered as a reference framework that will enable them to develop a diagnosis of their practices of Corporate Governance. It will also allow them to identify their main weaknesses in that respect and consequently, establish the necessary measures to improve their governance.

The Guidelines are a fully voluntary document, companies have the free choice to adopt it, motivated by diverse reasons, among which the willingness to manage their governance risks and help to achieve a greater sustainability.

Governance risk management is understood as the risk when inefficient governance affects the performance of the company. It is perhaps the strongest motivation a company may have when it comes to improving and strengthening its Corporate Governance.

Governance risks may emerge in different situations, for example and among others:

- Agency problems, or in short when the Board of Directors and/or senior management pursue objectives different to those of the shareholders.
- The formation of inefficient Boards of Directors (due to their size, structure, dynamics or a combination of the above) that do not exert their functions in the due form or do not constitute an effective counter-weight to management.
- The development of poorly planned processes for the replacement of the holders of key positions.
- Conflicts involving shareholders deriving from the absence of adequate mechanisms for communication or harmful practices affecting their equal treatment of these mechanisms.
- Deficiencies in transparency and in the disclosure of information.

Unfortunately, corporate history, especially since the global economic crisis that had its outbreak in 2007-2008, offers a significant number of cases of companies where Corporate Governance deficiencies, among other factors, have affected their value to the point some have disappeared. Perhaps the most paradigmatic cases known have occurred in the banking and financial sector worldwide, from the United States to Europe, where especially important cases have come to light. Nevertheless, there have also been cases of companies in all sectors of the economy, where a weak Corporate Governance has been the necessary cause of the loss of value.

Having reached this point, an urgent question arises: Should companies with a deficient structure and practices of Corporate Governance be penalized at the time of obtaining financing or resources? The answer to this question may be approached from the perspective of different actors:

- Capital markets
- Multilateral organisms

- Rating agencies
- Institutional investors
- Banking entities

In capital markets, and especially in stock markets, there are diverse cases in the region, such as the stock exchanges of Brazil or Peru, where specific market value indexes have been created for companies with good practices of Corporate Governance. The historical analysis of these indexes shows that investors consistently benefit from a price bonus and/or a lesser volatility when they own shares in these types of companies. This is consistent with the risk/profitability ratio, and seems to confirm that companies with a good Corporate Governance are in fact highly valued by the market, as they are perceived to have a small exposure to governance risks.

In addition, it is widely known that when governance risks begin to materialize, listed companies are penalized by investors almost immediately, given the liquidity of the market; on occasions this may turn out to be highly significant in terms of the risk level that becomes evident.

Thus, it seems reasonable to state that the actors in the capital markets do in fact take governance risks into account when they assess the value of listed companies, both in the positive sense and, especially, the negative one.

From the perspective of multilateral bodies, projects of long-term investment are more and more frequent in private companies but especially, in public ones. These types of organizations undertake a diagnosis on Corporate Governance, responsibility of their own team or external consultants, in order to determine the risks presented by governance of the company they are evaluating to investing in. There are even occasions when the team or external consultants recommend strengthening certain weaknesses of governance they have found within a certain time period, as an additional factor to consider when it comes to analyzing the operation.

This is a prudent position of the multilateral bodies, since their investments are usually long-term, of a significant volume, and are often structured in a complex form. This justifies undertaking an in-depth assessment of the company's risks, including those of governance. Except in very specific cases, rating agencies do not usually include components that place a positive value on good Corporate Governance practices when reviewing their methodologies.

However, what is considered in a generalized form in the rating methodologies of these agencies is that they penalize companies when they detect weaknesses of Corporate Governance; weaknesses that may imply a high governance risk or a risk not adequately managed. Consequently, it may be said that the rating agencies generally take governance risks into account in their methodologies, as a factor of penalization.

A variety of publications by institutional investors detail the important role these actors play in promoting Corporate Governance in the companies they invest in.

OECD, jointly with IFC, has published an interesting document about this matter: "**Strengthening**

Latin American Corporate Governance: the Role of Institutional Investor". This document is the result of broad discussions held for a number of years at the Latin American Corporate Governance Roundtable, where an analysis was made of the critical role these actors should play in the promotion and improvement of Corporate Governance in the companies in which they participate.

On this point, it is sufficient to indicate that institutional investors are usually key agents in strengthening the practices of Corporate Governance in the companies in which they participate. As professional investors who wish to protect their investments, they have a strong interest in promoting and strengthening Corporate Governance in the company in which they invest. Nevertheless, at least in the region, there are still certain gaps in compliance, that weaken the effectiveness of the role these type of investors should play.

All this leads us to conclude that, even though it may be in a heterogeneous way and with different levels of intensity, capital markets, multilateral bodies, rating agencies and institutional investors, do in fact take Corporate Governance into account when assessing the risk level of companies. The assessment of governance risks may affect the value placed on the company itself. In the cases of financing or investment transactions, it may affect their conditions in terms of time period, volume or the required profitability.

As a consequence, all of the agents previously mentioned play an important role, to a greater or lesser extent, in the effective promotion of Corporate Governance in companies. Thus, a given company's decision to strengthen its Corporate Governance may change from an absolutely voluntary and autonomous one to a decision, that on occasions, has been conditioned or motivated by these actors.

Nevertheless, the field of action of the actors mentioned is limited to listed or large-sized companies; it excludes the set of companies in the region that either do not participate in capital markets, either directly through the emission of freely quoted shares or indirectly through the issuance of fixed-income instruments, or do not incorporate institutional investors as shareholders.

It is in those companies, along with listed ones, that banking entities may play a key role in the promotion of Corporate Governance, both from their own individual perspective and to promote the improvement of Corporate Governance of their own clients.

A. Corporate Governance for banking entities

The recognition that the responsibility for the good functioning of a banking entity rests on itself, is the fundamental reason that justifies both, the need to have solid structures of Corporate Governance for these kind of entities, and the growing attention banking supervisors are paying to the aspects of Corporate Governance.

The role of Corporate Governance in the banking industry is crucial, given the following variables that characterize this sector:

- The complexity of banking risks.
- The dynamism of the sector.
- The high ratios of leverage with which it operates.
- The fact that the banking industry is based on trust.
- Systemic risk, that may not only affect the banking system as a whole, but also extend to the real economy, with serious macro-economic and social consequences, like the ones materialized during the global crisis of 2007-2008.

These reasons explain why the application of a series of good Corporate Governance practices, specifically aimed at banking entities is fundamental for any of these institutions, given also a class of creditors – the depositors – who deserve a strengthened protection.

That is why the Guidelines propose a concrete set of practices of Corporate Governance specifically applying to financial entities, in the form of guidelines and recommendations that form a reference framework with which they may undertake a diagnosis and define the main measures they should adopt to strengthen their own Corporate Governance.

In addition, and even though the Guidelines are not mainly aimed at supervisory agencies, the latter may be inspired by the contents of the Guidelines to consider including the Corporate Governance of the entities they supervise in their processes of supervision; it would be an additional element to take into account when they determine their risk profile and consequently, the degree of the supervisory agency's intervention.

B. Banking entities as agents for the promotion of Corporate Governance to their clients

The previous analysis lead us to believe that financial entities should probably begin to assess in their credit assessment methodologies the governance risks of the corporate clients, that is, the companies to which they provide financing. In the end, such corporate clients of bank assets are commercial companies that, like any other, are exposed to governance risks.

From the point of view of the banking entity, the relevance of this is that the individual governance risk of such corporate clients may also affect the banking entity itself. As a provider of financing, banking entities can observe how the materialization of governance risk of one of their clients affects the client's corporate performance. This could consequently have an impact on the client's compliance on the conditions of the repayment of the financing provided.

For that reason, the banking entity itself should be one of the key agents in the promotion of Corporate Governance in such corporate clients, so that it may rely on a better administration of governance risks by its clients and thus, be able to reduce its own degree of exposure to their governance risks. In short, it is a matter of improving the management and administration of the credit risks that the banking entities take in their activities; this being understood as the possible loss deriving from non-compliance with the contractual obligations their corporate clients enter into (borrowers or users of financing).

In line with what has just been stated, it is reasonable to suppose that if companies that implement sound practices of Corporate Governance show fewer risks than others with weaker governance structures, their risk premiums should be lower and thus:

- **From the perspective of the bank:** it presupposes a better administration of credit risks and thus, affects the calculation of risk premiums and the consumption of capital.
- **From the perspective of the company which takes financing:** since it presents a lower risk, it should obtain more favorable financing conditions.

Therefore, important advantages derive for the banking entity itself and for the companies borrowing money from it, in accordance with the following scheme:

- **Banking entity**
 - a) Better credit risks administration.
 - b) A more accurate estimate of risk premiums.
 - c) A more skillful technical management of the provisions.
 - d) Better perception by the market, by increasing their confidence in the bank's risk management.
 - e) Better administration of risks in general.
- **The company receiving the financing:**
 - a) Lower internal risks.
 - b) A higher market valuation.
 - c) The creation of intangible assets, mainly its reputation.
 - d) Ideally, lower financing costs and/or easier access to financing.

As a consequence, it seems reasonable to say that banking entities should become key agents in promoting Corporate Governance in the companies to which they provide financing. To this end, banking entities should include an analysis of Corporate Governance in their credit assessment methodologies, since the governance risks of the corporate clients could trespass to the banking entity itself. This way, banking entities would play a very important role in promoting Corporate Governance in the region, in line with the important role that capital markets, multilateral bodies, rating agencies and institutional investors already play.

C. The “MESEG” methodology for assessing governance risks of clients that receive financing.

CAF has been a pioneer in drafting a “Practical Guide for the Evaluation of Companies’ Governance Risk”, known as the MESEG (for its Spanish acronym). The MESEG does not go deeply into a complete **due diligence** for Corporate Governance, which would require the intervention of an external expert in the field of Corporate Governance. Instead, it provides a set of tools and criteria based on the principle of an expert opinion – a paradigm found in the Basel guidelines as the support for a modern supervision based on risks – to determine the governance risks of

a given company. It may be used by analysts who, without being experts in the field, will at least acquire a basic knowledge of Corporate Governance.

For that reason, the MESEG proposes a series of premises that will indicate the analyst when an in-depth **due diligence** should be carried out by an external expert, given opaqueness or governance risk has been detected in a given company.

While it might be thought that the optimum procedure would be to use a closed numerical system for the **scoring**, it is clear that Corporate Governance should be taken into account based on the particularities of each company. It also requires human input and expert opinion to evaluate the governance practices of the company.

The MESEG is a guide to the evaluation of the Corporate Governance risks of a company. It is made up of thirteen stages, to be followed in a sequential way. CAF, through its Corporate Governance program, makes it available to any interested banking entity.

Based on the Guidelines, we believe that the MESEG is an excellent tool that can and should be adopted by banking entities for their credit analyses. This way they can begin to assess the governance risk of the clients to whom they lend, and consequently, turn themselves into an actor of first rank in the effective promotion of Corporate Governance in the companies of the region.

Annex III. Corporate Governance in family enterprises

Strengthening the internal governance of family companies involves both the implementation of Corporate Governance practices to regulate the family enterprise as a company and the articulation of norms to organize the family business, mainly through the Family Protocol as its fundamental instrument.

With the use of a set of concrete tools, the application of Corporate Governance to family enterprises seeks to protect the company from turmoil that eventually could be originated on a family level, derived from questions of succession and generational change, and, situations associated with the relation between the family and the company (the inclusion of family members in the company, whether on the management level or the Board of Directors; the dividends policy; share transference and other issues).

Particularly, and from the Corporate Governance perspective, an essential tool is strengthening the Board of Directors of companies in terms of its composition, structure, appointments and the functions it performs, all of which directly contributes to enhance and protect the family enterprise.

From the perspective of the family, the definition and approval of a Family Protocol seeks to regulate and strengthen the family as a corporate family. The family will have clear rules in the future, for managing aspects such as succession, the inclusion of members of the family in the company, the role of the in-laws, etc.

Corporate Governance and family organization (through the Protocol) may be considered as two aspects that apply to different areas but are strongly interlinked and complementary between them. In this sense, the most recent studies of the subject have found that **family enterprises that have secured with success its continuity** have the following characteristics:

- First, they are companies that have secured the permanent strategic renewal of their **business** and the continued improvement and **professionalization** of management, on many occasions **thanks to the inclusion of the younger generation and/or external professionals**.
- In the second place, they have consolidated a **management and governance structure** (a Board of Directors, Family Council, Annual General Meeting) that is operative and effective, and has guaranteed the sound functioning of the company and respect for the shareholders' rights, both to information and retribution.
- Thirdly, they have promoted harmonious **family relations**, a fluid and constructive **communication**, as well as shared norms of behavior and respect to the company (that is, a **Family Protocol**) that have served to anticipate, manage and constructively resolve the conflicts encountered.
- Fourthly, they have had the ability to successfully **prepare successors from the following generation**, whether they are members of the family or external professionals who have been able to assume a gradual renovation of the leadership of the company's management, and promote the renovation of the strategic view of the company and the family.

- Last, the continuity of the family enterprise has **been directly assumed by the leaders of the family** who have considered this as a strategic subject.

Thus, such leaders have studied and sought advice about the generational change and on how to ensure the successful continuity of the company. They have devoted the needed time to that matter and have created a specific body (usually the Board of Directors or meetings with a consultant) to analyze the subject in a periodical and systematic way, and planned the process of generational replacement in advance.

Furthermore, and as a complement to what was mentioned, it has been shown that the most successful family businesses are characterized by a series of practices on the level of Corporate Governance and the level of family organization:

- On the level of Corporate Governance:
 - a) They have an **effective Board of Directors that includes members that are not part of the family** and has clear and defined functions. It is also responsible for the control and supervision of the senior management.
 - b) They adequately plan the **succession**, both of the CEO and especially, on the board level.
- On a family level:
 - a) The Family Council has **systematic meetings every quarter**.
 - b) They **periodically update the Family Protocol**.
 - c) They **clarify the responsibilities and salaries** of the family members who work in the company and own shares.

These Guidelines do not intend to be directed fundamentally to family companies. That subject is dealt in a CAF document specifically addressed to such firms entitled “*A Code of Corporate Governance for SMEs and Family Companies (Código de Gobierno Corporativo para las Pymes y Empresas Familiares)*”, published in 2011 and available on CAF’s institutional website for Corporate Governance: <http://scioteca.caf.com>.

Nevertheless, this should not be an obstacle to apply an adapted form of the contents of the present Guidelines to improve and strengthen Corporate Governance in family companies. Family enterprises face the double challenge of strengthening their structures and practices of Corporate Governance, to improve the company, and improve its family structure, to organize the family.

The sequence that should be followed to address these two dimensions may have a strong impact at the time of assessing the effectiveness of both processes.

In this sense, family organization is a long and complex process, in which the search for unanimity or at least very large majorities, is a key factor and may lead to temporary situations of blockage in specific areas.

Consequently, dealing first with the organization of a business family may lead to situations of blockage that may jeopardize the implementation of Corporate Governance practices aimed at protecting the family enterprise.

It is more effective and pragmatic to deal with the aspects of Corporate Governance and of family organization in a differential manner; the Corporate Governance aspects aim to strengthen the company while the aspects of organizing the business family are meant to strengthen the family, and are more likely to cause conflicts. Ideally, the total strengthening of Corporate Governance of the family company should be defined and ratified by a Family Protocol.

Now, it is important to highlight that approximately 85% of Family Protocols fail. Why? Basically, because families are not ruled or governed by papers, clauses or contracts, but by people. The Family Protocol should not be thought of as a simple document signed by all members of the family; what is really important is the process of communication, deliberation and agreement on which it is based. It is an ongoing process that requires well-structured bodies of family governance and suitable forums of communication. These will allow for the gradual consolidation of the company's family and above all, its preparation for the future.

As a consequence, the Family Protocol is the foundation of a true strategic plan for the family that deals with crucial themes like meritocracy versus family harmony, family values, the management of ownership and other matters. This will allow for the design of clear rules and the availability of solid criteria for the adequate management of family affairs.

The following six variables are very important at the moment of confronting the establishment of a Family Protocol that will maximize the possibilities of success.

1. The creation of the Family Protocol should result from the **express conviction and willingness of the family itself**.

If the creation of the Protocol is a response to external pressures, or only one member of the family is convinced of its usefulness, the possibilities that it will be a successful and effective document are drastically reduced.

2. The ideal moment to draft a Family Protocol is when there are no conflicts, that is, a time when the business is solid and the family's relationships are harmonious; this will facilitate a real and open discussion about the key subjects that will later be dealt with in the Protocol.

3. If that is not the case, it will be better to postpone the establishment of the Protocol and wait for a more favorable time, either in terms of the company or the family.

Participation in the creation of the Protocol must be as broad-based as possible, to facilitate the attainment of a wide consensus on the subjects of interest to the family.

4. The family should seek unanimity when it signs the Family Protocol. Otherwise family quarrels will arise sooner or later and may even become very serious; the very problem that the creation of the Family Protocol tries to avoid.

5. The elaboration of the Family Protocol should not be regarded as "checklist" of subjects, but a process where the important thing is to define, at least at the beginning, what matters need to be regulated or not.

For that reason, it is not a matter of going from 0 to 100, but attaining the maximum consensus

on the subjects dealt with, and leaving those for which no clear criterion is available for a later time.

6. The Family Protocol is a dynamic, living tool that necessarily needs to go adapting to the own evolution that the family and the company suffers.

That is why it is important to undergo it to periodical revisions. It should be adjusted to new circumstances that may arise and were not foreseen when it was created; either because they were not applicable or because there was no clear criterion for them and it was decided to leave them for later. In any case, the Protocol should fix the mechanisms and conditions to undertake those modifications in advance.

There is no single format for the Protocol; what is really important is the process set forth for attaining agreements on its contents. Nevertheless, the following broad areas usually form part of a Protocol:

A. The scope and objective of the protocol

This section introduces the fundamental reasons that motivate for the existence of the Protocol, as well as the nature and scope of the document. In some cases it will be very detailed and ambitious, and in others more generic, defining subjects to be left for the future.

The latter case applies to relatively young families, that have still not faced many of the situations a Protocol deals with and whose discussions are to be put off to a time when such questions are necessary.

B. The family business

This section tries to be specific about key aspects already forming part of the history of the company and family, and includes other information that may be necessary to provide criteria for dealing with future challenges. These include aspects such as the history, culture, mission, values, principles, leadership style, performance and role of the family and especially, its treatment of employees not members of the family. In this sense, it is important to reflect on the treatment and policies for executives and workers outside of the family; it is the cornerstone of the successful growth of the company in the future.

C. Governance bodies

This section determines and establishes the principles for separating the family and the company. For that reason, it deals with the creation or modification of the bodies governing both the company and the family, particularly:

- **The Board of Directors**, as the maximum body for governing the company, defining criteria for membership, requisites for becoming a director, the inclusion of family members and the functions and peculiarities of the Boards of Directors of family companies, etc.
- **The Family Council**, as the maximum body for governing the family, defining requisites for being a member, the areas it is responsible for, the rules of its organization and functioning, etc.
- **Other derivative bodies**, such as the family assembly, family day to day, etc.

D. The family-company relationship

This section deals with the main criterion that regulates this relationship, especially those to do with:

- **The inclusion of family members in the company**, starting with the conditions of entry to the company, training, promotion, salaries and the scope of their functions, among other matters.
- **Succession and generational turn-over**, especially with regard to the mechanisms that should govern the succession processes, both in management and ownership, a truly essential aspect in family companies.

E. The company-family relationship

This section sets policies related to:

- **The purchase and sale of shares in the hands of the family**, defining criteria that may facilitate solutions to situations of conflict or even blockage (especially referring to fixing prices mechanisms and the correct procedure for share transfer).
- **Decisions about dividends**, a key and often critical aspect for certain members of the family.
- **Share ownership and in particular**, whether or not to open the company's capital to people external to the family.
- **Share transfer**, establishing mechanisms for different scenarios, including *mortis causa* transfers, that may lead to the implementation of the Protocol to modify the arrangements made in the wills of the partners.
- **Other subjects** relative to the solution of conflicts the family decides to include.

F. Execution, compliance and modification of the Protocol

This section, that usually closes the Protocol, sets the way to put into practice the agreed-on decisions and the policies for approaching future modifications.

As was stated before, the Protocol is a living document that should gradually be adapted to the needs of the family. That is why it is crucial to establish how the Protocol may be modified in a way it honors its contents and at the time furnishes it with sufficient flexibility to adapt itself to the future development of the company, the family and the new circumstances and challenges they may face.

Finally, it should also offer a strong pragmatic approach to cases where the ownership of family companies is divided among different branches of the family. There would be different blocks of shareholders to regulate the regime for share transfers, the role of the different blocks of shareholders in the formation of the Boards of Directors, and the determination of the rights and duties of the shareholders.

For that purpose, a widely used tool is to draft **shareholders agreement** that regulates all of the previously mentioned aspects, as well as other relevant ones, in accordance with the specific circumstances of each family. The objective of this document is to define the actions of shareholders when

they exercise their property rights in the company. The document consequently, strives to protect the value created in the company, deriving from possible variables of a family nature that could affect the performance of the company's business.

Annex IV - Glossary of Terms

TERM USED IN THE GUIDELINES	DEFINITION
Majority shareholder:	In general terms, a shareholder who owns a majority of the ordinary shares issued by the company. In the strict sense, a majority means more than 50%, although in practice and depending on the stock structure and other variables, shareholders with less than 50% may come to control the composition of the Board of Directors.
Minority shareholder:	Titular holders of a small or relatively small number of shares in companies controlled by a majority shareholder. In some regulations, minority shareholders are defined as those who hold the title to less than 5% of the capital, although in companies with a very atomized capital, 5% may represent a very significant percentage.
Significant shareholder:	Shareholder of a company with a significant part of the capital (+ 10%), who normally has a stable character and may or may not hope to be represented on the Board of Directors. In companies with a large floating capital, a holding of between 3% and 5% may be considered significant. Significant may also be defined by the capacity to nominate and use his votes to elect a member of the Board of Directors.
Shareholders Agreement:	A written agreement that regulates the relationship among a group of shareholders with the objective of acting in a concerted manner and harmonizing their objectives, in order to safeguard their common interests. Depending on the percentage of capital represented by the shares of all those who subscribe to it, it may define the way of controlling and administering the company.
Administration of the company:	Acts and decisions made by the collegiate body of administration (the Board of Directors). Also understood as the governance of the company.
Agenda:	List of the topics to be dealt with at the Annual General Meeting, following the proposal of the Board of Directors – or chosen by the Board of Directors itself. Equivalent to the order of the day.
Senior management:	Group of persons responsible for the day to day management of the company, and in most cases, report hierarchically to the CEO. They are employed by the company and have the power to make general decisions about the management of the company. The senior management is made up of a series of executives led by the company's CEO, along with its internal auditor and general secretary.

TERM USED IN THE GUIDELINES	DEFINITION
Arbitration:	An extra-judicial procedure for the resolution of conflicts, except for those legally reserved to the courts. Equivalent to arbitral proceedings.
Annual General Meeting:	Meeting of all the shareholders of a company. Equivalent to general shareholders meeting.
Tag Along:	The right of minority shareholders to sell their shares simultaneously with controlling or significant shareholders in operations that imply a change of control of the company.
Right to withdraw or separate:	The right of shareholders who no longer wish to hold shares can have them purchased by the company at a given price, established in the law in certain pre-determined circumstances.
Director (board member):	A physical or legal person elected by the Annual General Meeting to act as an administrator of the company in his/her condition as a member of the Board of Directors. Equivalent to a counselor.
Board of Directors:	Collegiate body that administers a company. Equivalent to a management board or administrative council or directors' council.
Chief executive officer (CEO):	The Chief Executive Officer is the person with the maximum responsibility for the day to day management of the company, and to whom most of the members of the senior management report to. Holds a position in the company that answers directly to the Board of Directors.
Financial statements:	Group of documents the Board of Directors presents at the Annual General Meeting at the end of each financial year. Depending on the country, they include, among others, the balance sheet, the income statement, the management report, the annual report and the proposal for allocation of the year's results.
By-laws or "social by-laws":	Written document approved by the shareholders that assembles the most important internal norms of a company. Also known as the "social covenant" or articles of association.
Day to day or ordinary management of the company:	The ordinary business acts and decisions carried out by the company's senior management.

TERM USED IN THE GUIDELINES	DEFINITION
Relevant fact:	A piece of information that may reasonably affect an investor in the acquisition or transfer of securities or financial instruments. It may, thus, have a marked influence on their quoted price in a secondary market. Equivalent to news releases.
Privileged information:	Information of a concrete nature that directly or indirectly refers to one or several securities or negotiable instruments, or to one or several of its emissions. It has not been made public, and if it is made or has been made public, it may substantially influence or might have substantially influenced the market price of the security.
Institutional investors:	Professional investors, subject to a special regime of norms that regulate conduct and prudential supervision, who buy shares, usually on a stable nature, in the equity of companies and/or acquire debt instruments of issuing companies. Includes: pension funds, investment funds, mutual funds, the managers of these funds, insurance companies, banks, securities or brokerage firms.
Firms, companies or enterprises:	Legally-recognize entities made up of a group of natural or juridical persons that jointly place money, goods or industries in them, with the idea of obtaining a benefit, and are constituted in accordance with the commercial law of their domicile.

