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October 14, 2016

Securities and Exchange Commission
Republic of the Philippines
SEC Building
EDSA, Greenhills
Mandaluyong City
Philippines

By email: 2016cgcode@gmail.com

Re: Comments on Draft 2016 Code of Corporate Governance for Publicly-Listed Companies

Ladies and Gentlemen:

Cartica Management LLC (Cartica) appreciates the opportunity to provide comments on the SEC's Draft 2016 Code of Corporate Governance for Publicly-Listed Companies (the Draft Code).

By way of background, Cartica is an asset manager focused exclusively on emerging markets with assets under management in excess of US$2.7 billion. We operate a series of funds with a single active ownership strategy and a concentrated portfolio of listed equities. Our institutional client base includes some of the largest US pension funds and endowments as well as other sophisticated international investors. Currently, approximately 28% of our global assets under management are invested in companies listed on the PSE. Our senior staff, most of whom formerly worked at International Finance Corporation (IFC, the private sector investment arm of the World Bank Group), have considerable experience with the Philippines market. In particular, as a former advisor to the PSE on its aborted Maharlika Board experiment, the undersigned is especially acutely aware of corporate governance practices in the Philippines and has been closely following reform efforts in this area.

In order to facilitate the SEC's analysis of our reactions to the Draft Code, we have split our comments into two parts: 1) this letter, which emphasizes our most important objections to the contents of the Draft Code; and 2) the attached more extensive commentary, which follows the template provided by the SEC and includes section-by-section reactions.

General Feedback

In general, we find the Draft Code includes little to address investor concerns about the sorts of corporate governance outcomes that have caused the Philippines to consistently rank near the bottom of independent and well-respected regional governance rankings.[1] Many of its provisions are simply restatements of already well-recognized principles or existing law and regulation. Some provisions are so vague and general as to appear included merely to take up space or tick a box.[2] We fail to see how a timid repetition advances the cause of better corporate governance in the Philippines market or can be expected to tangibly improve

[1] Most recently in *ACGA/CLSA*, CG Watch 2016, Ecosystems Matter – Asia's Path to Better Home-Grown Governance, 2016, 3-6.

[2] e.g., Principle 15 on participation of employees.

governance outcomes. In particular, we see nothing in the Draft Code that will make it any harder for controlling shareholders and managers to engage in either of the two types of abuses that are justifiably of principal concern to investors in the PSE - *dilutive share issuances* and *abusive related party transactions (RPTs).* Nor does the Draft Code include recommendations that would provide minority shareholders with the means to protect themselves against such abuses.

A Fatal Flaw - Prevention of Effective Minority Shareholder Participation on Boards

By far the most concerning example of the Draft Code's timidity is its retention of the 2009 Code's provision excluding from the definition of independent director any holder of more than 2% of a company's shares.[3] We see no justification for this provision. It reflects a fundamental misunderstanding of the meaning of independence in markets, like the PSE, where most companies are characterized by identified control. In our view, and that of the vast majority of investors and experts, in markets with concentrated ownership the fundamental challenge of corporate governance is ensuring that the controllers, and the managers they appoint, act in the interests of all shareholders, and not solely in the interests of the controllers. The reason for requiring the presence of directors independent of controllers and management is to ensure that the Board includes members who can be relied on to act in the interest of all shareholders, untainted by the influence of the controllers. Accordingly, all directors and shareholders not connected with controllers and the management should be regarded as independent.

Furthermore, the 2% limitation for qualification as an independent director seems to us tailor-made to disenfranchise institutional investors with respect to the selection of independent directors. It would enable controllers to exclude from key committees, and probably from the Board itself, precisely those directors who would have both the incentives and the means to effectively look out for the interests of minority shareholders. The collective action problem of atomized shareholding is well-documented.[4] Retail shareholders do not have sufficient means or enough at stake to make it worthwhile to take an active role. Rather, it is significant minority shareholders (including institutional investors) who possess the financial and technical resources to look out for the interests of all minority shareholders and who have sufficient "skin in the game" to justify diligent oversight (including nomination of credible independent Board members). The Draft Code's provisions on independent directors effectively remove from the playing field the only potential parties that have the interest and resources to ensure a capable and motivated independent element on the Boards of PSE-listed firms, in favor of continuance of the current cadre of management-appointed independents with little capacity or incentive to "rock the boat". We therefore strongly urge the Commission to exclude these provisions from the final Code.

Dilutive Practices and Abusive RPTs

We also find especially disappointing that the Draft Code's misses the opportunity to address the current corporate governance regime's ineffectiveness in preventing the two types of abuses of principal concern to public shareholder in the Philippines: *dilutive share issuances* and *abusive RPTs*. [5]

Dilutive share issuances that benefit controllers (often dressed up as part of complex and opaque sets of transactions involving business combinations or "strategic alliances") are all-too-common practice in the

[3] The Explanations to Recommendation 1.2 and 5.2 of the Draft Code list beneficial share ownership in the corporation or its subsidiaries and affiliates exceeding 2% of outstanding capital as a reason for (temporary) disqualification of independent directors. We believe these provisions are unclear in their scope and would effectively bar institutional investors like Cartica from nominating and electing truly independent directors.

[4] *G20/OECD*, Principles of Corporate Governance, 2015, 23.

[5] These were confirmed yet again by recent independent research on governance trends in Asia: *ACGA/CLSA*, CG Watch 2016, Ecosystems Matter – Asia's Path to Better Home-Grown Governance, 2016, 184-185.

Philippines market. While the Draft Code gives lip service to the general principle of pre-emptive rights[6], there is scant recognition of the exceptions and work-arounds commonly employed by controllers that in practice limit its effectiveness. In this respect, we urge that the final Code recommend that companies request shareholder approval for new share issuances only when the full details of the anticipated transaction are fully disclosed (no open-ended pre-approvals) and that any waiver or exception to pre-emptive rights be approved by a majority of the minority shareholders. Similarly, we find the Draft Code's provisions on RPTs[7] generally vague and little more that restatements of existing (and ineffective) law.[8] Most importantly, there is no attempt to promote credible vetting of the fairness of material RPTs through a majority-of-the-minority approval requirement.

Overall, we do not see a serious effort to curb bad practices in these two crucial areas and simply do not see how the proposed "more of the same" approach reflected in the Draft Code will be effective in addressing the long-standing concerns of domestic and international investors in the Philippines market. The Draft Code would essentially continue to condone a governance framework that enables dilutive practices and abusive RPTs to continue to undermine confidence in PSE listed companies. We strongly urge the SEC to take a firmer stand by including in the final Code recommendations for truly robust oversight and approval mechanisms in line with international best practices and the realities of the Philippines market, and that have a real chance of tangibly improving governance outcomes.[9]

We thank the SEC for the opportunity to voice our concerns about the Draft 2016 Code of Corporate Governance for Publicly-Listed Companies. We hope that our comments will be taken into account in the Commission's deliberations on this topic. Please do not hesitate to contact the undersigned at +1-202-367-3011 or at mlubrano@cartica.com if you require clarification or have any questions about the issues discussed in this letter or the attached summary document.

Sincerely,

Mike Lubrano
Managing Director, Corporate Governance and Sustainability
Cartica Management LLC

[6] Explanations to Recommendations 13.1
[7] Recommendations 2.5, 3.5, 8.6, and 13.8.
[8] This is especially true for Recommendation 8.6 which, in our view, essentially requires firms to comply with existing law and is therefore unlikely to meaningfully improve governance outcomes.
[9] For further cross-country analysis of these two issues (including best practices) please refer to the following publications: *OECD*, Public Enforcement and Corporate Governance in Asia: Guidance and Good Practices, 2014; *CFA Institute*, Non-Preemptive Share Issues in Asia, 2014.

DRAFT CODE OF CORPORATE GOVERNANCE FOR PUBLICLY-LISTED COMPANIES

NAME: Mr. Mike Lubrano - Managing Director, Corporate Governance and Sustainability

REPRESENTED INSTITUTION: Cartica Management LLC

PART of the CODE of CORPORATE GOVERNANCE	COMMENTS	PROPOSED CHANGE
Disqualification of Independent Directors - Recommendations 1.2 and 5.2 and Explanations	These provisions retain the 2009 Code's provision excluding from the definition of independent director any holder of more than 2% of a company's shares. We see no justification for this provision. We believe it reflects a fundamental misunderstanding of the meaning of independence in markets, like the PSE, where most companies are characterized by identified control. In our view, and that of the vast majority of investors and experts with experience in markets with concentrated ownership, the fundamental challenge of corporate governance is ensuring that the controllers, and the managers they appoint, act in the interests of all shareholders, and not solely in the interests of the controllers. The reason for requiring the presence of directors independent of controllers and management is to ensure that the Board includes members who can be relied on to act in the interest of	We strongly urge the Commission to exclude these provisions from the final Code.

	all shareholders, untainted by the influence of the controllers. Accordingly, all directors and shareholders not connected with controllers and the management should be regarded as independent. Furthermore, the 2% limitation for qualification as an independent director seems to us tailor-made to disenfranchise institutional investors with respect to the selection of independent directors. It would enable controllers to exclude from key committees, and probably from the Board itself, precisely those directors who would have both the incentives and the means to effectively look out for the interests of minority shareholders. The collective action problem of atomized shareholding is well-documented. Retail shareholders do not have sufficient means or enough at stake to make it worthwhile to take an active role. Rather, it is significant minority shareholders (including institutional investors) who possess the financial and technical resources to look out for the interests of all minority shareholders and who have sufficient "skin in the game" to justify diligent oversight (including nomination of credible independent Board members). The Draft Code's provisions on independent directors effectively remove from the playing	

	field the only potential parties that have the interest and resources to ensure a capable and motivated independent element on the Boards of PSE-listed firms, in favor of continuance of the current cadre of management-appointed independents with little capacity or incentive to "rock the boat".	
Board Composition - Recommendation 1.2 and Explanation	Most PSE-listed firms are controlled by an individual or a group. In this context, only Boards with a majority of independent directors can ensure effective oversight of management. However, the draft provisions fail to encourage firms to appoint majority-independent Boards or to limit the number of executive directors. Instead, the provisions call for an "appropriate mix" of non-executive and executive directors. The Draft Code therefore does not adequately recognize the importance of a strong independent Board.	We urge the Commission to encourage firms to appoint a majority of independent directors and to discourage them from appointing any executive directors other than the CEO.
Related Party Transactions (RPTs) - Recommendations 2.5, 3.5, 8.6 and 13.8 and Explanations	We are similarly concerned that the Draft Code fails to address the current corporate governance regime's ineffectiveness in preventing abusive RPTs. We find the Draft Code's provisions on RPTs generally vague and little more that restatements of existing (and ineffective) law.	We urge that the final Code recommend that companies perform credible vetting of the fairness of material RPTs through a majority-of-the-minority approval requirement. In addition, only independent directors should be eligible to sit on the RPT Committee.

	Most importantly, there is no attempt to promote credible vetting of the fairness of material RPTs through a majority-of-the-minority approval requirement. Furthermore, the Draft Code fails to comply with international best practices by not calling for the RPT Board Committee to be composed of independent directors only.	
Board Committees - Recommendation 3.2	We find it particularly concerning that the Draft Code does not call for the Audit Committee to be entirely composed of independent directors. The provision fails to comply with international best practices in this area and we do not see why these standards should not be implemented in the Philippines market.	The final Code should call for the Audit Committee to be entirely composed of independent directors.
Over-Boarding - Recommendation 4.2 and Explanation	Recommendation 4.2 of the Draft Code reflects the well-recognized principle that individuals who take on too many directorships ("over-boarding") cannot devote sufficient time and attention to adequately perform their duties. However, the Draft Code fails to distinguish between individuals who hold a full-time management position in a company, and those that do not (e.g., "professional directors"). We believe that if an individual is a full-time executive in a company, he or she cannot	The final Code should recommend that an individual serving in a full-time executive position should sit on the Board of at most one other company.

	possibly have the time to sit on the Boards of five other companies. Such individuals should be limited to serving on the Board of at most one other company.	
Management Committee - Recommendation 5.2 and Explanation	The provisions list membership of "management committees of the board of directors" as a reason for disqualifying independent directors. However, management committees are not listed under Principle 3 (Board Committees) or in the introduction and therefore, we do not know what the provision refers to.	We request that the SEC either precisely define the role of management committees in the final Code or drop the reference to it under Recommendation 5.2.
Lead Independent Director - Recommendation 5.5	International best practices generally call for the designation of a Lead Independent Director in cases where the Chair of the Board is not independent, including cases where the roles of CEO and Chair are held by the same individual. The Draft Code rightly calls for the designation of a Lead Independent Director in cases where the roles of CEO and Chair are combined. However, the Draft Code fails to specify that this should cover any scenario where the Chair is not independent.	The final Code should recommend that firms appoint Senior Independent Directors in any scenario where the Chair of the Board is not independent.
Informational Rights of Independent Directors - Recommendation 5.7	Independent and non-executive directors need to have direct access to internal audit and	The final Code should encourage firms to schedule separate meetings between independent directors and the heads of

	compliance functions to effectively perform their oversight functions. The Draft Code rightly calls for separate meetings between non-executive directors and the heads of internal audit, compliance and risk functions. However, the Code fails to establish a similar provision for independent directors.	internal audit, compliance and risk functions without any other (executive or non-executive non-independent) directors present.
Company Disclosures - Recommendation 8.3	In Cartica's experience with the Philippines market, the ultimate beneficial owners of shares are not generally fully disclosed. The Draft Code recognizes this and encourages firms to disclose these details. However, we are skeptical whether establishing such provisions on a "comply or explain" basis will be sufficient in meaningfully improving disclosure practices.	We request that the SEC actively monitor disclosure practices and consider making public disclosures of ultimate beneficial share ownership practical and mandatory.
Company Disclosures - Recommendation 8.6 and Explanation	The provisions simply restate relevant law and regulations of the SEC, BSP and PSE without adding additional requirements that could improve governance practices.	We urge the SEC to drop these and all other redundant provisions in the final Code.
Non-Financial Reporting and Sustainability - Principles 10, 12, and 16 and respective Recommendations	The provisions establish important general guidelines regarding sustainability but fail to adequately recognize ESG issues in the context of firms' risk management systems.	The final Code should include material ESG risks in its provisions on risk management systems (Principle 12).

	Market participants increasingly recognize the central importance of actively managing material ESG risks. However, the Draft Code does not list ESG risks under its provisions on risk management systems (Principle 12). We therefore do not see how the Draft Code will encourage firms to manage their ESG risk exposure in a forward-looking way.	
Dilutive Share Issuances - Recommendation 13.1 and Explanation	We find especially disappointing that the Draft Code's misses the opportunity to address the current corporate governance regime's ineffectiveness in preventing dilutive share issuances. Dilutive share issuances that benefit controllers (often dressed up as part of complex and opaque sets of transactions involving business combinations or "strategic alliances") are all-too-common practice in the Philippines market. While the draft code gives lip service to the general principle of pre-emptive rights, there is scant recognition of the exceptions and work-arounds commonly employed by controllers that in practice limit its effectiveness.	We urge that the final Code recommend that companies request shareholder approval for new share issuances only when the full details of the anticipated transaction are fully disclosed (no open-ended pre-approvals) and that any waiver or exception to preemptive rights be approved by a majority of the minority shareholders.
Employees' Participation - Principle 15, Recommendations 15.1	The provisions are so vague and general as to appear included merely to take up space or tick a box. We fail to see what they add and their vagueness is an invitation to mischief.	We request that the final Code replace these vague provisions with more specific mechanisms to encourage employee participation in line with international best

		practices such as Principle IV. C. of the OCED Principles of Corporate Governance.
Anti-Bribery and Whistleblowing - Recommendation 15.2 and 15.3	The draft provisions are vague and fail to outline clear and robust anti-corruption and whistleblowing guidelines. Furthermore, the structure of the provisions is unclear and we fail to see why these two important responsibilities of the Board are addressed under Principle 15 (Employee Participation) and not under Principle 2 (Roles and Responsibilities of the Board).	The final Code should clearly define the Board's leadership role in ensuring risk oversight and the integrity of the firm in line with OCED Principles of Corporate Governance (Principle VI. D. 7). It should also mandate robust commitments to anti-corruption and whistleblowing through firms' risk management systems (Principle 12 of the Draft Code).