Voting Policy when Operating a Proxy in General Meetings

For the years 2017 – 2018

Entropy Financial Research Services

April 2017

For Convenience Sake,

Entropy's voting policy is concentrated in this document

The document is an integral part of its Annexes, which include an Introduction, Legislative Background, Accepted Practice in the World and Statistical Data

1. Appointing the Board of Directors and its Composition

1.1 Ratio of Independent Directors

A. Standard: We will recommend that at least a third of the Board members will be independent or external Directors**.**

B. Exceptions according to the Ownership Structure and the Size of the Company: Taking into account the ownership structure in the company, we will recommend appointing more independent Directors with preference to External Directors as much as it is relevant in respect to the law.

C. Additional Reservations:

- **In companies with span of control –** We will recommend appointing at least a third of the Directors in the Board to be Independent Directors (based on their definition in the Companies Law).
- **In companies without span of control –** We will recommend appointing at least 50% of the Directors in the Board in companies without span of control, to be Independent Directors (based on their definition in the Companies Law).
- **Chairperson of the Board of Directors** – will not be counted as an independent Director.
- **Criteria to be classified as Independent –** The following will be checked: the tenure of the candidates as Directors in the company (a Director serving as a Director for over 9 years will be defined as Dependent, except in the cases of dual-listed companies and foreign companies with no controlling interest); the role of the candidates as office holders and/or as consultants in the company or in the companies group, their business and family connections with stakeholders in the company and every position or occupation which may cause a conflict of interests.
- **A Director who serves as a consultant to the Management –** Will not be counted as an Independent Director, therefor we will recommend the receiver of the consultation be the Board of Directors and not the Management in order to avoid conflicts of interests in providing the service.

1.2 Quantity of Family Members

A. Maximum Number of Family Members: We will recommend opposing appointments of Directors who are family members of the controlling shareholder, over a third of the quantity of Directors, including the controlling shareholder himself.

1.3 The Size of the Board of Directors

A. **Maximum Size of the Board of Directors:** The size of an effective Board of the Directors, should be maximum 13 members (except for financial and banking corporations that are required to abide by additional strict regulation requirements)**,** and that of course according to the size and the nature of the company's activities.

B. **The Size of the Board of Directors in Small Companies**: A large number of Directors, when this is not needed, may weigh on the company's ongoing operations and cause redundant expenses. Therefore, in the case of small public companies, this issue will also be reviewed under cost –benefit considerations.

1.4 Staggered Board of Directors

As part of the voting policy, we will recommend opposing mechanisms of Staggered Boards of Directors as well as appointments of Directors within such a framework. We believe that this mechanism does not serve the interests of all the shareholders since it deprives them of their basic right to appoint Directors in reasonable intervals of time and to review their conduct while in service, while protecting the Directors and the controlling shareholders (if there are any) who serve as Directors. In addition, the Staggered Board is known as having a negative effect on the value of the company, especially when combined with a "poison pill", a strategy which is relatively easy for a Staggered Board to adopt.

2. The Competence of Directors and their Independence

2.1 The Competence of the Board Members

A. **Reviewing competence based on the directives of the Companies Law:** In principle, our recommendation will be based on the directives of the Companies Law on this matter, including the declaration of the candidate as to the existence of the required skills and checking their ability to dedicate the required time for the fulfillment of the job, considering the special needs of the company and its size.

B. **Directors' Trainings**: We recommend that the company makes efforts to routinely check the Directors' competence and the trainings they need in order to fulfill their job and to cope with professional subjects related to the activities of the corporation, the needs of the capital market and other general subjects.

C. **Publishing the Training Program**: We recommend that this training program be published so that the shareholders will be able to review it. This recommendation aims to strengthen the corporate governance elements in the corporation.

2.2 An Appointment of a Director or an External Director Suggested by an Institutional Investor

A. Encouraging Institutional Investors to suggest a Candidate: In view of the increasing need to enhance the trust of the investors in the Board of Directors, we believe it is appropriate to encourage institutional investors to suggest a candidate of their own to the position of a Director or an External Director.

B. Supporting a Candidate Suggested by an institutional Investor: In case that in a general meeting an institutional investor suggests a candidate for the position of a Director or an External Director[1] while on the other hand the Board of Directors suggests another candidate who is supported by the controlling shareholder, we will recommend voting for the candidate who is suggested or supported by the institutional investor, assuming of course that this is an appropriate candidate from all aspects.

C. Supporting the Decisions of an External Director Suggested by Institutional Bodies: In order to encourage the actual appointment of the candidate who has been suggested by an institutional investor to the position of an External Director (in view of the veto right held by the controlling shareholder in votes of the general meeting against a candidate suggested by minority share holders to the position of an External Director for a first tenure), we believe it is best to have more trust in the discretion of the Remuneration Committee, the members of which have been suggested by institutional bodies and are supported by them. Therefore we will tend to provide a positive recommendation to decisions in matters of remuneration, being brought for the approval of the general meeting, in the tenure of an External Director who has been suggested by institutional bodies, as long as this External Director actually supported the remuneration decision and it does not essentially contradict the principles of the voting policy.

2.3 Extending the Nomination Period of a Director

When extending the nomination period of a Director, the following main issues will be considered:

A. The Service Period of the Director: In principle, we will act according to the definition in the Companies Law and will **classify the Director as Dependent in a service of over 9 years,** except in cases as detailed in article B below.

[1] The Companies Law grants a minority investor who holds at least 5% of the company's shares the possibility to ask to call a special meeting, and an investor who holds 1% of the company's shares to ask to add an appropriate subject for discussion to the agenda of a general meeting which has already been called, up to a week after the date the meeting has been published.

B. **In Dual-listed companies and in Israeli Companies Traded Abroad, which have a Decentralized Ownership[2]:** We will classify a Director as independent even if they served as Directors for over 9 years[3], assuming the company's Board of Director's structure complies with our policy for companies with no controlling shareholder (Over 50% of the Directors are independent) and that we are confident that the Director's long time in office does not affect their performance and the performance of the Board.

C. **Rate of Attendance in the Board of Directors meetings:** We believe that the shareholders are entitled to expect that the candidates attend a minimum of 75% of the Board meetings and committees they have been nominated to, in at least two years prior to the date of the nomination (in as much as the Director served in the company during that period), where we will apply the threshold of at least 75% attendance for each year separately.

D. **Inspecting the Voting Record of External Directors:** When nominating an External Director[4] we will also wish to inspect the voting record of the said External Director in sensitive transactions where they are an essential gate keeper (transactions with controlling shareholders and essential remuneration issues). In view of this, we will examine the decisions of the Board of Directors on issues of remuneration and essential stakeholder transactions made in the period of the External Director's service, and all the circumstances, including the way the External Director voted in these decisions, as far as there is open information on the subject. In as far as the External Director supported decisions which drew significant negative votes from institutional bodies, we will consider this fact and calculate it in our recommendation regarding the nomination.

E. **Using an External Independent Advisor:** At the time of re-nomination of a Director, and especially when re-nominating an External Director, and in accordance with the circumstances of the matter, we will check to see to what extent the Director could, pending the existing needs, use external independent counseling on various professional essential subjects which they needed in order to do their work. We will also investigate who is the entity in charge of approving this budget, whether there is a policy on this

[2] With no controlling shareholder.

[3] See also regulation 5A(b) to the Companies Regulations (Relaxations for Public Companies whose Shares are Registered for Trading on an Exchange Abroad), 5760-2000.

[4] Nominating an External Director for a first period of service requires a simple majority and also a special majority while nominating for a second and third period can be done in a special majority only, meaning by the approval of only the minority shares holders, article 245(a1)(1) of the Companies Law. Hence the position of the minority shares holders is very important when nominating for the first period and also when re-nominating.

issue and more. This information will be presented to the shareholders in the framework of our recommendation, in as far as the information in open.

2.4 Restricting Service in Several Boards of Directors in Parallel

A. Restricting Service in Several Essential Boards of Directors: We recommend restricting the number of Boards in which a suggested Director may serve to 6 essential Boards of Directors[5], another factor which will be considered is whether the Director has an additional significant occupation on top of their occupation as a Director in companies.

B. A parallel service in other companies in the group, including in subsidiaries and subsidiaries of subsidiaries, will not be counted in the number of essential Boards of Directors, in as far as their business activity is not deviating from the activity of the company / the group.

2.5 Appointing a CEO as a Director

Notwithstanding the need to keep the Board of Directors separate from the Management, we will recommend appointing the CEO as a Director in the company for the following reasons:

- The service of the CEO as a Director will obligate them with additional responsibilities and will diminish from their ability to evade legal responsibility for actions they have brought for the approval of the Board by claiming they have no formal status in its approval.
- Business wise it is appropriate that the CEO who is leading the practical management and as such initiates most of the issues brought to the approval of the Board of Directors (except for the issue of control over the performance of the actual management, which has to be performed periodically without the presence of the CEO), will also take part in the decision made in the Board of Directors.
- In certain circumstances, the absence of the CEO from the Board of Directors may cause estrangement, misunderstandings and unnecessary conflicts between the Board and the Management.

2.6 Appointing a CEO who is a Controlling Shareholder as a Director

We will recommend supporting the appointing of a CEO who is a controlling shareholder as a Director in the company, pending the existence of balancing control mechanisms in the Board of Directors, which enable controlling the work of the CEO in their absence.

[5] An essential Board of Directors is a Board of Directors of a public company and/or of a private company with an essential scope of activities or significant complexity in the structure of activity. Information regarding private companies will be based on public information channels and on the reports of the company. This restriction in being applied as of September 2014 and is being reviewed on an annual basis.

Our position stems from our understanding the an addition of a Director on behalf of the controlling shareholder in order to create the said separation of roles, does not always improve the corporate governance and sometimes even creates an unnecessary expense and the "expulsion" of the controlling shareholder from the Board of the Directors, a situation which is not optimal because of the dominancy of the controlling shareholder and their strong influence on the Board. As opposed to it, applying appropriate control mechanisms, will lead to improving the efficiency of the Board's work, contribute to the internalization of the need for appropriate control and supervision mechanisms on the work of the CEO (as detailed in the recommended Corporate Governance Regulations for conducting meetings without the attendance of the CEO in order to review their performance in their absence, which we will encourage applying in these companies), and also decrease the risk inherent in the operation of a Board of Directors in a company with an active controlling shareholder, who is not a member in it.

2.7 Appointing Office Holders who are reporting to the CEO as Directors

As a rule, we recommend opposing the nomination of office holders or other managers who report to the CEO, as Directors in the company.

2.8 Separating the Role of the CEO from the Role of the Chairperson

A. **Serving as a CEO and as a Chairperson in Parallel:** In view of the unique control structure in the Israeli market, which is characterized by multiple controlling interests, and the influence of this structure on aspects involving the independence of the Board of Directors, we recommend as a rule to oppose situations of parallel roles as CEO and Chairperson and we also recommend to oppose the appointment of a CEO, or any of the persons reporting to them, or any of their family members, to the role of the Chairperson of the Board of Directors, in parallel to their role as the CEO of the company.

B. **Exceptions:** However, we will reconsider our position only in the following exceptional cases:

- **A temporary appointment:** In cases where there is a justification for a temporary parallel service, such as in crisis management, bridging over a transition period etc. (providing the parallel appointment is for a short period).
- **Family companies:** In exceptional cases only, in which the company presents a significant surplus contribution for the shareholders and over a long period (at least 5 years), and after increasing the rate of the External Directors to a level of 50% of the Board of Directors, as a compensation for the non-separation of the roles of the Chairperson and the CEO.

- **Companies with no controlling interest** (relevant mainly to dual-listed companies or to companies traded only abroad with no controlling interest): We will consider recommending a parallel service as Chairperson and CEO in cases where there is no controlling shareholder in the company and also if we find that the Board of Directors has balancing mechanisms which enable efficient control over the work of the CEO as Chairperson, such as: the existence of a Lead Independent Director[6]/[7], the existence of a Nomination Committee, a clear explanation regarding the need for a parallel service and inspection of the extent to which the Board in independent.

3. Reliefs and a Special Reference to Types of Corporations

3.1 Small Companies

In continuation to the initiative of the Securities Authority to create an outline of reliefs for small companies and out of a wish to encourage their development and growth and turning them into significant companies, we chose to **encourage the segment of the small companies in a way that will make it easier for them to handle themselves in the different aspects of corporate governance.**

A. **Defining the Criterion for being a Small Company**: The following points refer to companies whose market value is lower than NIS 50M (hereunder: **Threshold Conditions**) in an average calculation of 90 days prior to the date set for attendance in the meeting. When required, additional parameters will be taken into account such as shareholders' equity, revenues, the value of the company in recent years and the extent of the free float.

B. **The Guiding Principle for Extending the Reliefs**: It will be applied on a case by case basis, where the guiding principle is that changes will be required in cases where the size of the company and its structure will uniquely require it and after we will be satisfied that the economic benefit and the essential rational in the case of the said company are positive and that the removal of the following mechanisms, in the present point in time, is

[6] The status of the Lead Independent Director has been regulated in 2002 by the New York Stock Exchange and has become very strong in the last years in the American market. Today, this status has been established in almost all the big American companies, over and above the original requirements of the stock exchange. The growth in the scope of this phenomenon stems mainly from the fact that it serves as a counterweight to the existence of CEOs who serve as Chairpersons in American companies http://www.pwc.com/us/en/forensic-services/assets/lead-director-survey.pdf

[7] ISS policy for 2016 details the roles of the Lead Independent Director and indicates that the nomination should be from among the Independent Directors and that it should include a detailed definition of their roles including: (A) To lead all the meetings of the Board of Directors where the Chairperson is absent, (B) To be used as a link between the Chairperson and the Independent Directors, (C) To approve information submitted to the Board of Directors, (D) To approve the agenda of the Board of Directors and to make sure that enough time is provided in order to discuss every issue on the agenda, (E) A full mandate to call meetings with the attendance of the Independent Directors, (F) To promote creation of direct communication with the main shareholders from the public. https://www.issgovernance.com/policy-gateway/2016-policy-information/

not expected to lead to an essential damage to the corporate governance factors in the near future.

C. **The Relief Sections**: Following are the changes which will be considered in regards to companies that fulfill the Threshold Conditions above:
   - Appointing a Chairperson as a CEO – Will be made possible when it is made clear that the value of having one person in the role of CEO and Chairperson is required and does not essentially affect the corporate governance fabric in the company and that there are alternative control means.
   - The Structure of the Board of Directors – A deviation from the principle of an independent component of not less than 1/3, will be made possible.
   - The restriction of maximum 3 family members serving in the Board of the Directors will be removed.
   - The prohibition on appointing an office holder to be a Director will be removed.
   - The possibility to appoint the same person to serve as a Chairperson and CEO for a period defined in advance will be considered favorably.

D. **Encouraging the Nomination of Directors Suggested by Institutional Investors**: On the other hand and as a balancing factor, Entropy will encourage, especially in these companies, nomination of Directors which will be suggested by institutional investors as part of the right granted to them by the Companies Law, pending the competence of the Directors and their independence and the additional over for their service that we conduct.

3.2 Companies in lists for Retention, Suspension and Removal from Trade

Many dozens of public companies in Israel today are in a retention list, have been suspended or removed from trade. This situation inflicts harm on the shareholders and the value of their shares, because the public shares become non-tradable and non-liquid and the institutional investors who hold them are burdened with high holding costs. In addition, in these public companies there is an increased risk of abuse against minority shareholders, as the managers of the company to not feel any moderating market effect. The main interest of the public shareholders in these companies is relisting the shares for ongoing trade in the stock exchange.

Checking the Actions and the Efforts the Company Performed in order to return to the Trade: We will check the actions and the efforts the company performed in order to restore its listing prior to the meeting, actions such as: using a market maker, distribution of shares, connections with investors, etc. In every case that a company is in a list for retention,

suspension or removal from trade and where there is a motion on the agenda of a general meeting to ask the minority shareholders to approve remuneration to the controlling shareholder or their relatives or a re-nomination of a Director in the company, we will consider recommending to oppose the motion if we get the impression that the company did not do enough in order to restore regular trading activities.

3.3 Public Limited Partnership

On February 23, 2015, the Partnership Ordinance[8] has been amended and for the first time a chapter regarding the rules of corporate governance which apply to public limited partnerships, has been added to the ordinance. Several limited partnerships are being traded in the Israeli stock exchange, dealing mainly with the Energy sector, and up until this amendment they have conducted themselves without any corporate governance rules which are regulated by legislation. In view of this, Entropy published in June 2015, a Position Paper on the subject "The Involvement of Institutional Bodies in view of the Amendment to the Partnership Ordinance Law (No. 5), 5775-2015", which presented the role of the institutional investors in the assimilation of the change to the rules of the corporate governance in partnerships. The rules of the corporate governance for a public limited partnership, which have been set in the amendment to the ordinance deal with a variety of issues, such as: limitations in the matter of the areas of activity of the company of the general partner; nomination rules, competence and loyalty obligations of the Directors at the general partner; the obligation to nominate an Audit Committee, External Directors, an Internal Auditor and an auditing CPA; the obligation to nominate a supervisor, their authorities and liabilities; approval of a remuneration policy and approval of stakeholders' transactions; instructions in the matter of retaining the capital in the partnership; and instructions in the matter of offers to purchase all shares and merger into the public limited partnership. The corporate governance rules defined for a public limited partnership resemble the corporate governance rules for public companies, since usually the issues the rules deal with are similar. However, it is important to remember that the limited partnership has a corporate structure which differs from the corporate structure of a company[9]. Because of these differences, the new law extends the rules of the corporate governance to apply also to the general partner company, which manages the partnership, and orders the nomination of a supervisor to be chosen only by the participation unit holders who have no personal interest.

[8] A law to amend the Partnership Ordinance (No. 5), 5775-2015, book of laws 2490 dated Feb. 23, 2015.

[9] Among other things, the control in the partnership is a buttressed control of the controlling shareholder in the company of the general partner and it has no connection to the percentage of capital held by the controlling shareholder, the limited partnership itself has no Directors and the holders of participation units have a limited ability to influence the management of the partnership.

A. **Voting Policy in Partnership Matters which is Identical to the Standard Voting Policy**: Generally speaking, the voting recommendation in meetings of participating units' holders in a limited partnership will be according to the guidelines of Entropy's standard voting policy.

B. **Encouraging Institutional Investors to suggest candidates**: We will encourage institutional investors to suggest appropriate candidates for the post of the Supervisor on the limited partnership and to the post of External Directors in the general partner company.

C. **Supervisor's Term of Service**: Because of the concern regarding the lack of independence, we will recommend not to approve the continuation of the office of the supervisor for a period of over 9 years, but will favorably consider a personal rotation of the supervisor from the same CPA firm or the same lawyer's firm.

4. Compensations for Senior Personnel

4.1 The Remuneration Subjects Included in the Voting Policy

We will review the fairness of the compensation package based on the rating of the Corporate Governance Risk of the issuer as well as the Entropy Model for evaluating the fairness of the remuneration, in view of the economic value of the whole wages package, including all its components, while considering the business results of the company and its performance, including the performance of the shares over time and also, in case the compensation package is target based, we will review these targets.

A. In 2016 we have started publishing on behalf of our customers, Corporate Governance Risk Ratings as part of the expert opinion service towards the general meeting, out of our wish to assimilate the use of corporate governance considerations in the voting considerations of institutional investors towards the general meeting. This change is an integral part of the Entropy policy regarding the importance of empowering the role of the Board of Directors and encouraging the appointment of professional and independent Directors in order to contribute to the improvement of the corporate governance in the company.

Extending the issues on the agenda of the shareholders' meeting in view of the last amendments to the law (16, 20 and the Law for the restriction of the remunerations to senior personnel) and the requirement for a supermajority in approving remuneration and salaries, stem in our view, from a decrease in the trust between the shareholders and the management of the company and its Board of Directors. In view of that, in every case

where we estimate that the company presents an appropriate conduct for a long time period and that the level of its corporate governance is high, we will encourage managerial flexibility and give a higher weight to the discretion of the Board in general and the Remuneration Committee in particular, in setting the targets and the scopes of the compensations to office holders.

Therefore, in order to enhance the connection between appropriate considerations at the vote in the general meeting and the corporate governance level in the company, we have decided to include in the recommendations towards the general meeting, considerations which are essentially the level of the corporate governance in the company calling the meeting.

Therefore, as of the date of the publication of the voting policy for 2017, in cases where the corporate governance score is at least "Advanced", when the criteria set out in regards to the articles which are coming up for discussion do not significantly deviate from the guidelines set out in Entropy's policy, we will calculate the subject of the corporate governance in a way that will lead to a positive recommendation in regards to remunerations to office holders on the agenda and in regards to additional subjects dealing with the structure and quality of the Board's work.

B. Using a Peer Group: If needed, and especially in cases of relatively high sums of remuneration, we will compare data with a peer group (which is usually a group of companies with similar characteristics in terms of activity and value) and will provide our opinion in regards to gaps, if there are any, compared to the peer group. We will grade the peer group in two dimensions:

- **i.** The size of the compensation package in comparison to the peer group
- **ii.** The performance levels in accordance to economic performance indicators which are suitable to the nature of the company's activities.

We will estimate the gap between the relative position of the company in terms of the size and the development of the compensation package relatively to the peer group, and its position in terms of performance indicators and the performance of the shares of the companies in the control group for at least the last three years and the extent of the adequacy between them.

According to our worldview, the lack of adequacy between the size and the development of the compensation and the company's performance in these tests makes it necessary to adjust the compensation in terms of structure and size in order to improve it. We wish to emphasize that while a deviation from what is common in the sector is a reason to oppose

the compensation, defining the compensation in accordance with what is common in the sector, does not ensure supporting the compensation, because it is possible that the level of compensation in the sector is too high, or that the connection between remuneration and performance as common in the sector is too loose.

C. **The Time to Bring the Terms of the Remuneration to the Approval of the Meeting**: We believe that an employment agreement with an office holder, which requires the approval of a general meeting, needs to be brought to the review and approval of the shareholders prior to the commencement of their work and not after the fact. However, we will review this in view of the particular circumstances and as long as the interim period between the time of the employment and the approval of the meeting is not too long.

D. **The Formula of the Compensation**: We recommend that the compensation formula be defined in advance and that it does not change after the fact, while giving the Board of Directors reasonable discretion in the implementation of the compensation, including the ability to reduce the size of the compensation. We recommend building a compensation package in a simple and easy to understand way, as complex and multi-components compensation packages may miss their target.

E. **We will evaluate the extent to which the remuneration caps have been used, especially where there is no open information in regards to the varying components linked to the actual performances of the company in the three years preceding the date of the re-approval**.

F. **Deferred Payments**: We will execute caution when referring to deferred payments (such as benefits after retiring), which may hide the size of the actual compensation.

G. **Varying Remuneration linked to Performances**: Beyond a reasonable basis salary, the compensation needs to be linked to performance, desirably in a linear way and with no one time additions.

H. **Increasing the Remuneration Towards Retirement**: We believe that increasing the remuneration towards the retirement should not take place (including payments in return for a commitment not to compete with the company after retiring).

I. **Using Relative Rather than Absolute Performances**: We will encourage companies to use remuneration linked to relative performances in comparison to the performances of the sector or the stock market indices rather than linked to absolute performances. In the case of options, companies can use the realization price linked to a stock index that the Remuneration Committee will define, or decide that the realization is pending the

achievement of relative performance targets (for example targets pending on profits) that the Remuneration Committee has set up.

J. **Reviewing Compensation in a Dual-Listed Company with a Decentralized Ownership Structure or an Israeli Company Traded in foreign Stock Exchanges:** When reviewing a request to approve a compensation policy in a dual-listed company or in an Israeli company traded in a foreign stock exchange, we will especially focus on investigating the performances of the company in the three years preceding the date of the approval of the policy and we will also check the remuneration practices which have actually been implemented by the Board of Directors. If we find a positive correlation between the performances of the company and its remuneration practice, which is evidence to a reasonable and responsible Board of Directors, we will recommend supporting the approval of the compensation policy even if the compensation policy does not have threshold provisions or measurable quantitative forward looking targets.

K. **Supporting Decisions of an External Director who has been Nominated by Institutional Bodies:** In order to encourage the nomination of a candidate who has been suggested by an institutional investor (in view of the veto right of the controlling shareholder in the general meeting to overrule a vote for a candidate suggested by the minority shareholders for the position of an External Director in a first term) and in view of the increasing need to enhance the trust of institutional investors in the Board of Directors, we will tend to grant more trust in the discretion of the Remuneration Committee and we will also give a positive recommendation to the decisions on issues of remuneration which are submitted for the approval of the general meeting in the term of service of an External Director who has been suggested by institutional bodies, as long as this External Director really approved the remuneration decision and it does not essentially contradict the principles of the voting policy.

4.2 Fixed Remuneration – Salary and Various Payments

A. **Publishing an External Consulting Work (Benchmark):** Without expressing any opinion whether it is appropriate to use benchmarking, in case the companies relied on an external consulting work which included a peer group for benchmarking and if the size of the compensation is in the upper range of the common market practices in the company's sector, we will recommend that the companies publish the external consulting work in order to produce transparency in regards to the range of considerations and information items submitted to the Directors when they considered the approval of the remuneration policy or a personal remuneration agreement. In addition, we will recommend that the

consultation work includes information about the performances of the company as compared to the sector or the selected peer group, so as to enable checking the correlation between the position of the remuneration and the position of the company's performances.

B. **Deviation for a Cap or a Range defined in the Policy:** In case the company chooses to define a cap or a range, we will check the extent of the deviation, if there is any, between the defined cap and the levels of the wages in the company as the case may be.

C. **Approving the Wages Plans After-The-Fact**: We recommend opposing the approval of wage plans after the fact. The remuneration rules in general, including rules regarding bonuses, are supposed to be defined only in advance and there will be no remuneration, unless the formula and the conditions to its calculation have been agreed upon in advance, but for a discretional component of a reasonable size.

D. **Signature Bonuses and Golden Parachutes**: Will be calculated as part of the cash payment component, in the total cost of the remuneration plan.

E. **Advance Notice Period for Office Holders**: We will recommend not over six months, considering the company's performances, the structure and details of the remuneration, unless in this time period the office holders are committed to provide actual services to the company.

F. **Increasing Compensations Close to the Retirement Date**: We will recommend objecting to increases in compensations close to the retirement date and also to payments in return for commitments for no competition after the retirement, which have been submitted for approval close to the retirement date.

G. **Guidelines on the Issue of Severance Packages and Adjustment Periods** – We will recommend to add a limitation to say that the size of the combined severance package and/or adjustment grant together will not exceed six wage months, this in addition to the advance period which is limited to up to six months. In extraordinary circumstances, in addition to a significant contribution of the office holder, a long service period and the appropriate restrictions of non-competition, we will consider a deviation from this threshold.

4.3 Medium Term Compensation – Bonuses

We view financial bonuses as something which should be provided pending upon fulfillment of targets, which should be defined in advance. The targets have to be adjusted to the company's characteristics and the areas of its activities. We believe that it is preferred that the rate of the bonus out of the set targets, should be linear. In addition, in certain cases, especially in case it is an office holder who is a controlling shareholder, it is required to set a normative margin, where only above that margin, the bonus will be granted.

A. **Neutralizing Revaluations and Extraordinary Events:** In case a profitability target has been set, we believe that if the bonus is linked to the net profit, then it should reflect the results and as far as possible, after neutralizing revaluations and extraordinary events which are mainly accountancy events which do not reflect supplementary performances of the office holders (compensation based on revaluations which are based on future streams, with low probabilities, may result in granting bonuses which do not conform with the real performances).

B. **Compensating Performances based on a Long Term View:** We believe it is right to base compensation components on performances, with a long term view and it is not appropriate that a financial bonus will include extraordinary performances which are not within the scope of the company's activity or which stem from an influence external to the company, revaluations based on low probability future streams and also that there will not be payments of bonuses in regards to the completion of purchase transactions, but rather a remuneration which has an incentive due to the success of the transaction, which can be provided by means of capital components for example. It is appropriate that the bonus plan be a multi-year plan, so that it may setoff over-performances with underperformances during the plan years. Part of the bonus has to be distributed forwards, so that it is deferred to the next years and future payments will be executed pending on fulfillment of targets. We will especially emphasize this subject in individual compensation agreements, and in cases of office holder who is a controlling shareholder or their relative.

C. **A Quantitative Threshold to the Bonus:** In view of the clear need to keep the confidentiality of business information, and as a result of this, the obvious difficulty of companies to provide quantitative details on their targets in the compensation policy, and the need for transparency of the compensation mechanisms towards the shareholders, we believe, that it is at least appropriate that the company sets up a relevant and effective

quantitative threshold provision which will serve as a transparent "power cutter" for the shareholders for payment of bonuses.

The effectiveness of the threshold provision stems from its being linked to a leading index which represents the company's performances in a good and reliable way and from its level that should be set up in consideration of the performances of the company in the last three years and of the special circumstances of the specific sector. For example, if there is an expectation for essential or other regulatory influences.

D. **In Extraordinary Cases, Publication of Targets in Regulation 21**: In extraordinary cases, where the company has difficulties in setting up and publishing an effective quantitative threshold provision, it will be possible to detail the quantitative targets after the fact, within the framework of regulation 21 in the financial statements and the level of their fulfillment along the details on payments of bonuses actually made.

E. **CEO Remuneration**: A varying remuneration pending performances for a CEO will be based on measurable and well defined criteria, except in cases where it is a non- essential part of the overall remuneration.

4.4 Aspects of the Financial Reporting Regarding Payment of Bonuses

In every case in which the shareholders in the company do not have the ability to calculate the actual sum of the bonus using the bonus formula as approved in the general meeting (i.e. if the index is composed in a way that makes it impossible to extract its values in a simple way from the financial statement), we will recommend publishing complementary information within the framework of regulation 21, so that it will enable a better certainty in regards to the completeness and the reliability of the calculation which was used for the actual payment of the bonus.

A. **Disclosure Requirement**: The disclosure requirement is the practical way to know if the bonus paid really abided by the decision of the general meeting in as far as it was a complex calculation mechanism.

B. **Nullification Order in Case of Nondisclosure:** The order to nullify the approval of the general meeting acts as a sanction and ensures that the disclosure requirement is acted upon.

C. **The Reference of the Auditing CPA:** Since regulation 21 applies to the Board of Directors' repot that is not being audited by an external CPA, the reference of the auditing CPA is needed in order to create a controlling means regarding the correctness of the calculation.

D. **Reporting in the Framework of Regulation 21 in the Periodical Report:** In view of the fact that sometimes the paid bonus is based on accounting indices from which all sorts of components are neutralized, we will insist on the existence of a clear and transparent reporting under regulation 21 in regards to the way in which the bonus has been calculated[10] as detailed below:
   - Per the regulation there will be a coordination between the unified net profit attributed to the shareholders and the decisive annual profit for the calculation of the bonus, including listing the sums comprising this coordination.
   - Also, per the regulation, there will be details on the annual bonus calculation, based on the decisive annual profit for this calculation.
   - In addition, the said report will include a presentation of the Board of Directors that the auditing CPA has provided the company with an unreserved and without paying attention opinion, according to which the above coordination and the calculation of the annual bonus are appropriately represented, in all essential aspects.
   - The inclusion of the said details in the periodical report is an essential and fundamental condition to the approval of the annual bonus.

4.5 Capital Remuneration

Upon the provision of capital remuneration we will recommend that the conditions of the program form an appropriate incentive to act in order to maximize the long term value of the company. We believe that a capital based remuneration helps in reducing possible conflicts of interests between office holders and shareholders and thus to motivate the office holders to act for the good of the company and for the good of the long terms policy considerations, while taking risks in a controlled manner. This reasoning gets weaker when the said office holder is one of the controlling shareholders in the company, and in accordance, we believe also the real justification of capital remuneration to controlling shareholders is weakened.

A. **Parameters to be Reviewed:** We will review the rational and the reasons on which the grant is based, we will consider the question whether the remuneration plan has been composed after considering other alternatives and we will review the provisions of the plan, including: the extent of the expected dilution, its economic value, the realization prices and the vesting period.

B. **Price of Options' Realization:** In case the capital component is options, we will recommend opposing such a capital bonus that represents an immediate benefit "in the money" or which are "near the money". For that matter we will review the average price

[10] Only in case this is a complex mechanism which does not enable a simple calculation with means which are open to the investor.

of the share during a representative period prior to the date of the provision. The subject will be considered while taking into account the volatility of the share at that time.

C. **Restricted Stock Based Remuneration:** In case this is a capital component which is in essence granting of shares, we will recommend supporting restricted stock and/or restricted stock units (RSU) based remuneration, in as far as their provision will be conditioned upon relevant performance targets which are relevant to the nature of the company's activity such as the achievement of return targets, etc.

D. **Recalculation of Options to Employees, Directors and Senior Office Holders**: In regards of reducing the price of realization of options, we will review this on a case by case basis while addressing the following subjects:
   - We will check the time lapsed from the time the options have been granted, the period of time left until the expiration date and also the vesting and expiration dates following the change.
   - We will refer to the dilution extent following the change and the cost of the change to the company.
   - The time lapsed from the beginning of the deterioration in the price of the share up to the date of the recalculation, is recommended to be over a year.
   - We will expect that in case the recalculation includes a change in the price of realization of the options, then the new realization price should be equal to or higher than the top price of the share in the year preceding the date of the recalculation.
   - We will check to see if the decrease in the price of the share is directly linked to underperformances of the company and its managers or if it depended to a large extent on exogenous variables.

E. **Limiting the Maximum Possible Accrued Dilution Extent, Due to the Total Awards Granted in the Company**:
   - For companies in the TA 100 Index, we recommend limiting the dilution to around 10%.
   - For companies in the Yeter (rest of the shares) Index we recommend limiting the dilution to around 15%.
   - In plans designed for all the employees and in plans of R&D companies (as defined in the rules of securities stock exchange) we will consider a higher dilution.
   - In varying market conditions, the calculation of the dilution percentage will be performed while considering the gap between a theoretical dilution and an actual dilution.

F. **Terms of Allocations to the Chairperson and the CEO**: In regards to the terms of allocating benefits to the Chairperson and the CEO, the realization price and the terms of the plan have to form an appropriate incentive for them to act to maximize the long term value of the company. In accordance to this, we will recommend, in accordance of the specific circumstances, to set up an appropriate premium on the actual price of the share and/or incentive enhancing targets as a condition to the vesting/ provision of the restricted options and/or stock units, and in accordance to the said above in regards to maximum dilutions.

G. **Relief to companies in Retention or Protection of their Condition:** In certain companies, such that are in the process of retaining their business or protecting their business condition for personal reasons or reasons stemming from their business environment, or if it is a case of negligible extent, we will support allocation of options for office holders in a realization price which is near the money, which are based on an average of the 30 last trading days at least. In cases where a premium is required at the time of the allocation, it will be considered in accordance with internal indices which have been developed at Entropy and include for example the expected dilution extent, the phase the company is at and the its expected growth, its business condition, the extent of tradability and volatility in the company and more, on the basis of which the need for a premium and its range will be determined at the time of the allocation.

H. **The Vesting Period:** The proper vesting period should not be less than three years (or partial realization over the years).

I. **Realization Period:** The proper realization period should not be less than a year after every vesting period. The dilution ratio between the senior personnel and the rest of the employees should be tested for reasonability.

J. **Evergreen Mechanism**: We recommend opposing an option plan which includes an evergreen mechanism (an automatic renewal mechanism).

K. **The Nature of the Capital Remuneration in Banking Corporations:** In banking corporations, in view of the critical importance of the issue of the risk appetite and the instructions of the Supervisor on this subject, we will recommend supporting a restricted stock and/or restricted stock units (RSU) based remuneration in as much as their provision is pending performance targets such as achieving return targets, capital adequacy, etc. However, we believe that the recent legislation regarding the remuneration in the financial sector will decrease the motivation to compensate office holders by capital means.

L. **Sole Discretion of Directors:** We recommend opposing the provision of sole discretion rights to Directors in regards to changing the option terms, including in regards to recalculations.

M. **Options in the form of "Poison Pills":** We recommend opposing the provision of options/shares in the form of "poison pills".

N. **An Immediate Acceleration Mechanism:** We recommend opposing automatic mechanisms which enable immediate acceleration of the provisions of a capital award, except in cases of changing of control or significant events which may provide value for all shareholders. In certain such cases, we will consider supporting the acceleration of the terms of a capital award, provided only that this is not an office holder who is a controlling shareholder.

O. **Provision of Options in an Affiliated Company:** The provision of options in an affiliated company will be reviewed in accordance to the extent to which the office holder is involved in the business of the affiliated company.

4.6 Remuneration to Senior Office Holders in the Financial Sector

The law restricting the remuneration to senior office holders in the financial sector[11] includes significant limitations on the extent of remuneration to senior office holders in financial corporations, and specifically it sets a ceiling of NIS 2.5M per annum[12] on wages and does not allow approving a remuneration which exceeds the limit of 35 times the lowest wage of any employee.

In regards to remuneration to senior officers in the financial sector, our position will comply with the law.

In regards to remuneration policies in other sectors, we will continue to apply the principles of the voting policy while addressing and conforming to the norms prevailing in the market following the adoption of this law. In addition, we intend to build a new model aiming to review the fairness of the remuneration, and thus it will measure in a more significant way the connection and the correlation between the performances of the corporation and the suggested remuneration, and will be an indication as to the nature of the recommendation in regards to this remuneration.

[11] Remuneration Law for Office Holders in financial Corporations (A Special Certificate and Prohibition on Tax Deductions due to Extraordinary Remuneration), 5776-2016.

[12] The main principles of this law include: (1) A remuneration cap of NIS 2.5M per annum, where provision of payment over that cap requires special approvals of the Remuneration Committee, the Board of Directors in a special majority which includes a majority of the External Directors or the Independent Directors; and the general meeting, with a special majority which includes the majority of the minority. (2) It will not be possible to approve a remuneration which exceeds 35 times the cost of the lowest earning employee in the corporation (including contractors' workers). (3) An expense of a corporation due to a remuneration which exceeded the remuneration ceiling of NIS 2.5M, will not be tax deductible.

4.7 Remuneration to Directors and External Directors

Since the control structure in corporations in Israel is characterized by controlling shareholders who concentrate in their hands a significant part of the capital of the company, our approach regarding the role of the External Directors is for them to be, among other things, a counterweight against the controlling shareholders. Therefore, their remuneration's extent and type have a significant importance.

A. **Remuneration to Directors Above what is Set Forward in the Regulations**: In cases where this is a professional Director, or an expert providing a unique contribution to a company which is requested to compensate its Directors at extents which are higher than set forward in the companies' articles on the subject of remuneration to External Directors in view of the business environment the company operates in, we will recommend supporting it. This attitude is in accordance with our approach in favor of reducing parallel service terms of Directors and the need to fairly compensate them for their service if required to reduce parallel offices.

B. Paying a salary which is higher than the said in the articles in regards to External Directors' remuneration, will be reviewed against the general principles of remuneration to office holders.

C. **Double Payments to an Office Holder who is a Director**: We will oppose provision of additional remuneration to office holders who serve as Directors over the remuneration paid to them for their service as office holders.

D. **Varying Remuneration**: Varying performance based remuneration paid to Directors, will be based on measurable well defined criteria, except for cases where this is a non-essential portion of the overall remuneration. A component which does not exceed 20% of the fixed annual remuneration will be considered a non-essential portion for this matter.

E. **Directors in Financial Bodies**: In regulated financial bodies, banking corporations and insurance corporation, the remuneration payments to Directors (except for the Chairperson) will be fixed and will be determined according to the External Directors' remuneration regulations.

F. **Chairperson of a Board of Directors in a Financial Body**: The remuneration of the Chairperson of the Board of Directors in a regulated financial body, will be only a fixed remuneration, which will be determined in relation to the remuneration of an External Director, according to the type of the financial body, its size, the extent of complexity of the job and the amount of hours on the job.

G. **Chairperson's Remuneration**: We will recommend supporting a Chairperson's remuneration which reflects a reasonable ratio against an External Director's remuneration, where as of today in insurance companies and in banks it ranges between 18 and 20, but is expected to essentially decrease in view of the essentiality of varying components in the ceilings of the remunerations today, which are prohibited according to the new legislation.

4.8 Directors and External Directors' Capital Remuneration

External Directors' remuneration by capital means is common in developed capital markets in the world, as part of the perception that the interest of the Director and all the other shareholders has to be enhanced in order to maximize the value of the company.

A. **Parameters for the review of the External Directors' Capital Remuneration**: We will support the allocation of capital components to External Directors when reviewing it on a case by case basis and while addressing the following considerations:
   - A Maximum Ratio of the Fixed Remuneration: The company will determine in its remuneration policy or when calling the meeting for the approval of the remuneration, a maximum ratio between the rate of the capital remuneration and the fixed remuneration to Directors, so that it will not exceed 50% of the fixed annual remuneration, including payments for meetings.
   - Allocation and Vesting Periods: The capital remuneration will be allocated for a period of three years at least with a vesting period of the first portion of at least two years.
   - Preferred Components: We will recommend giving preference to capital components which encourage a restrained risk appetite like for example restricted stock and/or restricted stock units, rather than options.

B. **External Directors in Financial Bodies' Capital Remuneration**: In regulated financial bodies, banking corporations and insurance bodies, the Directors and External Directors do not have a varying capital remuneration component.

4.9 Salary Payments to Office Holders in a Corporation made by a Controlling Shareholder

We recognize the concerns the controlling shareholders have regarding the difficulty in today's market to remunerate office holders to extents which were common in the past and now, in view of the current trends, it may prove to be difficult to approve. However, there is some concern that since the remuneration to the office holder is not disclosed but rather being conducted by the company towards which the office holder is committed to be loyal and prudent, this may harm the adequacy of the interests they are supposed to apply in regards to all the shareholders of the company.

Revealing the details of the remuneration: In view of the pioneering nature of the issue of "Salary Payments to Office Holders by a Controlling Shareholder" in our policy, we will recommend that the company discloses the details of the remuneration of the office holders, in order to make sure that it does not contradict the remuneration policy of the company, which applies to all office holders, all that in accordance with the intentions of the sixth addition to the securities Regulations[13].

5. Management Agreements

Our recommendations regarding management agreements between public or private companies in the control of the controlling shareholder and a public company they control.

A. **Criteria for the Review of the Management Agreements:** We will review management agreements according to their extent and their worthiness to the company, and among other things, according to the size of job, financial extent in relation to operational parameters of the managing company, consulting services to affiliated companies and comparison to similar companies and to what is common in the market. In the process of approving the management agreements, the possibility of direct payment will be reviewed. The direct cost to the company providing the management services will also be reviewed and the costing of the services will be done back-to-back against this cost.

B. **Providing a Full and Detailed Report on the Cost of the Services and their Nature:** We will oppose signing a management agreement in every case where the shareholders do not get a report which includes a full and detailed description of the services, their extent, the costs involved in each and a description of the office holders providing the services.

C. **Restricting the Period of the Management Agreements:** It is best that management agreements be restricted to up to three years.

6. Mergers, Acquisitions and Transfer of Activities

In mergers, acquisitions and transfer of activities, we will review each case separately, while especially focusing on the unique characteristics of the transaction. We will check the rational and the economic aspects of the transactions from a long term perspective, with a basic

[13] Section 21 of the Securities Regulations (Periodical and Immediate Reports) 5730-1970 requires adding to the periodical report a detailed table regarding the remunerations to senior officers. The section refers to the sixth addition to these regulations. Section (3) of part C of the sixth addition states: "If the remunerations table includes remunerations provided by an entity which is other than the corporation, including a corporation in its control or the controlling shareholder in the corporation, the identity of that entity must be revealed in addition to the extent of the remuneration they have provided."

assumption that long term interests of the company are the same as the interests of the shareholders.

A. **The Structure of the Transaction**: We will also address the structure of the transaction, the dilution potential, if there is any, and its probability.
B. **Level of Transparency**: We will inspect the level of transparency in essential transactions, and especially the transparency in aspects such as the price of the transaction, external value valuations, due diligence documents, pro-forma documents, etc.
C. **Abusing the Rights of the Shareholders:** We will check if in the structure chosen for the transaction, the shareholders have appropriate protection and if the transaction's structure may lead to abusing their rights in relation to other shareholders. We will especially focus on transactions for the removal of public companies from trade by means of a reverse triangular merger.
D. **Costs Due to the Transaction:** We will pay attention to payments and wages involved in the transaction and in the transfer of control.
E. **Appropriateness of the Process**: We will review the appropriateness of the negotiations process in the transaction, whether the company checked alternatives and whether significant negations in order to improve the terms of the transactions, have been conducted.
F. **Reviewing the Interests of the Controlling Shareholder**: We will check if the controlling shareholder in the company has a personal conflicting interest in approving the transaction or if the terms of all shareholders of the company were equal.

7. Transactions of Stakeholders

In principal we have reservations regarding transactions with stakeholders, however, and in view of the fact that the law allows such transactions, in view of their necessity in some cases, we will, in the framework of the proxy policy, review transactions with stakeholders very carefully on a "case by case" basis. We will inspect both the question if there is justification for the transaction with the stakeholder in general (instead of a transaction with a third party or avoidance from any transaction) and the question if the terms of the transaction promote the interest of all the shareholders in the company (and not only if they are not harmful to them).
The following rules will be fully applied only in essential transactions of acquisition/sale/merger with the controlling shareholders in the company.

A. **Conducting a Competitive Process by the Audit Committee**: The default option in handling stakeholders' transactions is that the Audit Committee or a sub-committee nominated by it will conduct a competitive process in the market. If the Committee finds that such a process should not be held, then it must provide reasons and afterwards at least

conduct vigorous and exhaustive negotiations with the controlling shareholder. The committee will be able to choose consultants and experts, who are not consulting the company or the controlling shareholder in general or in the said transaction, and will get help only from consultants and experts it chose as described. At the end of the process, the committee will decide whether to support the transaction. While the committee is in the negotiations and reviewing process, it should not rely on negotiations held by the management of the company and not on opinion papers the management of the company or its legal advisors ordered.

B. **Reviewing the Appropriateness of the Transaction:** In most transactions, the review will focus on the appropriateness of the process which led to the decision to close a deal with the controlling shareholder and on the way in which the terms have been formulated. In this framework we will ask for the following information: Why is the transaction needed; have other alternatives in the market seriously been looked into; have the terms of the transaction been formulated in real negotiations between an independent committee of the Board of Directors and the controlling shareholder; on what has the committee based its agreement to the final outline of the transaction and does the report submitted to the general meeting, where the transaction will be voted upon, detail in full transparency all the things the minority shareholders need in order to decide whether the transaction is good for them.

C. **In Capital Stake Gaps of the Controlling Shareholder, the Inspection will be Stricter:** As an initial indication towards the inspection the transaction, as far as there is a gap between the capital stake of the controlling shareholder in the transaction's object in relation to their capital stake in the company they are stakeholders in, as the case maybe, we will conduct a more rigid inspection. If the capital stake is the same in both, then the initial inspection will be simpler in view of the fact that the concern regarding the abuse of the control structure against the minority shareholders, declines.

D. **Complete Details on the Phases of the Process:** We will check and make sure that the transaction report disseminated towards the general meeting describes in detail the phases of the process:
   - The transaction's background
   - The legal tool chosen for the transaction, especially if the alternative was a Reverse Triangular Merger against an Acquisition Offer, which is in principle the better option in our view.
   - The way in which the independent committee and its advisors (value valuators and legal advisors) have been nominated.

- The progression of the competitive process in the market, and if such a process has not been conducted, the explanation of the committee as to why it has decided to give it up.
- The progression of the negotiations between the controlling shareholder and the committee.
- The changes made to the outline of the transaction and the explanations for the changes.
- The steps taken in order to check other alternatives
- The way in which alternatives suggested by third parties have been dealt with

E. Ensuring that the Minority Got the Best Profit Achievable from the Transaction[14]: Entropy's policy states that the controlling shareholder bears the burden of convincing that the transaction is better for the minority than its alternatives **(**avoidance from making a transaction; a similar or other transaction with a third party; another transaction with the controlling shareholder). Within the review one has to ensure that the minority gets the best profit achievable from the transaction.

F. Whenever the know-how of the Entropy team in a transaction submitted for its approval is insufficient, Entropy will choose an external expert consultant who will work on behalf of the minority shareholders in the said transaction. Their wages will be received from the company calling the meeting and paid back-to-back by Entropy when their work is finished. Note that if the company refuses to appoint an external expert as described, without reasonable reasons, we will recommend rejecting the transaction.

This policy is substantiated by the power given in amendment 16 to the Companies Law, to the minority shareholders and the development of the legislation since then. In the decision of the District Court in Tel Aviv-Yafo in the matter of ***Kahana vs Makhteshim Agan Industries*** *from 2011, dealing with a merger between the parent company and a subsidiary, it has been stated that in order to ensure the fairness of the transaction, the terms of the transaction have to be determined in an actual negotiation, not just for the sake of appearances, between the controlling shareholder and an independent committee of the Board of Directors, that will have the authority to decide against the transaction, that the representatives of the controlling shareholder will not be present in it and that it will be able to use experts and advisors which are not dependent on the controlling shareholder. The court emphasized the importance of transparency in regards to the decision making process and the process of filtering the suggestions which would eventually be submitted for the approval of the general meeting.*

G. In certain types of transactions we will need more than the disclosure of the steps taken in order to check other alternatives to the transaction in the market, but rather insist

[14] The Concentration Law changed in an indirect amendment (no.22) of the Companies Law the requirement that a stakeholder transaction be approved only if it does not cause harm to the company, to a requirement that it be approved only if it is for the good of the company.

that these steps are taken. The Concentration Law, in the indirect amendment (no. 22) to the Companies Law, requires that in cases of controlling shareholders' transactions (even if they are not extraordinary transactions) the Audit Committee must conduct a competitive process supervised by whoever it chooses and by criteria it will set forward, or to decide on conducting other processes as it defines, prior to carrying out these transactions, and all in accordance to the type of the transaction. The Audit Committee may determine criteria once a year in advance, for this matter. In addition, the law requires that the Audit Committee determines what controlling shareholders' transactions which are not extraordinary, are also not negligible, and to determine the way they will be approved, including also to define transaction types which are not negligible that will need the approval of the Audit Committee. The Audit Committee may decide on the said classification in regards to types of transactions by criteria that it will set forward once a year in advance. We consider the conducting of a competitive process an important tool for ensuring the good of the company.

8. Capital Structure

8.1 Increasing the Registered Share Capital

When deciding to increase the registered share capital of the company, the shareholders must approve it in a general meeting with a regular majority, unless the articles of the company state otherwise (in companies that have not changed their articles following the application of the Companies Law in Feb. 1, 2000, the required majority is 75% of the attending parties).

Requiring the Approval of the Shareholders: A public company is conducting this process for time to time and uses the share capital in order to raise more capital, increasing capital based remuneration plans and exploiting opportunities in the area of mergers and acquisitions. We believe that this process is an integral part of the ongoing management of the company's business. The requirement to seek the approval of the shareholders enhances their ability to control future allocations.

8.2 Capital Allocations/Issues

A decision regarding the allocation of convertible shares, options and bonds is usually in the hands of the Board of Directors.

Reviewing Unfair Capital Allocations: We will conduct stricter inspections in cases of unfair capital allocations which can potentially abuse the rights of shareholders, and we will especially give attention to the following issues:

- The terms of the offer in relation to the fair economic value.

- The extent to which the allocation is needed and its rational from the point of view of the company and the shareholders.
- Checking alternative options for the allocation and its terms.
- Maximum dilution of the existing shareholders.

8.3 Changes in the Issued Share Capital

Decisions regarding changes in the issued share capital, capital consolidation and capital sub-divisions, require the approval of the shareholders. We will focus on the issue of the value of this decision in terms of simplification of the trade in the stock exchange and the enhancement of the tradability of the securities, while addressing the terms of the change and its cost for the shareholders.

9. Dividend Payouts

On the decision making process regarding dividend payouts, we will apply additional tests aimed to extract the appropriate profit for payouts, which abides by the repayment ability tests based on a higher probability levels of the flow as indicated by the accounting profit as detailed below:

A. In view of the ever increasing early adoption of the IFRS standards by Israeli companies, and since they effect the profit reserves of the company in ways which may sometimes artificially increase the profit appropriate for payouts by the present law, we will recommend performance of additional tests in order to determine the appropriate profit for payouts in order to avoid a situation which may lead to the weakening of the capital basis of the company in a way that may negatively affect the return production capabilities of the company in the future and cause harm the shareholders.

B. The dividend payout, as well as the return on investment, immediately increases the overall return the shareholders get as a result of their investment in the security. Companies that have a clear payout policy, which is applied consistently, are companies which enjoy excessive pricing by their investors.

C. However, sometimes the payout decision is based in considerations which do not abide by the good of the company in the medium-long term, considerations of capital needs in the group and/or among the controlling shareholders.

D. The Companies Law allows dividend payouts even when the company has accrued debts, in case the company had profits in the last two years. It is possible to pay dividends with the approval of the court in cases where the balance of the reserves is lower than the total payouts or even negative, provided that the court has been convinced that the payout will not negatively affect the future repayment ability of the company. In view of this fact, we

have decided on several rules regarding the evaluation of the amount of dividends payable for the purpose of an appropriate application of the test of repayment ability.

E. The maximum possible dividend payout (without a special approval from court) is the sum complying with the profit test according to section 302 of the Companies Law.

F. Based on the terminology of the IDRS standards, the profit test is applied as the part of the shareholders of the paying out company (excluding the part of the minority) in the profit/loss before other general profit – the accrued balance (balance of surpluses) or the sum accrued in the last two years, according to the highest (and all of course after deducting dividends which have already been paid out).

G. The sum of dividends actually paid out has to be smaller than the sum put to the profit test, if the sum put to the profit test, includes essential revaluations. For this matter, the term "Revaluation", refers to every adjustment to the value of assets or liabilities (both upwards or downwards), which has been included in the sum put to the profit test and where the cash flow indicated by it is not certain actually. The principle is that as more the cash flow indicated by the revaluation is less certain, the sum of the dividend actually paid out should be smaller.

H. The certainty level of the cash flow as indicated by a revaluation in a given sum, depends on:

- The length of time expected until the realization of the asset or liability revaluated;
- The probability that by the time of the realization of the asset or the liability revaluated, there will happen an inverted change in the base upon which the revaluation has been done (fair value, recoverable value, currency rate, index, etc.) and-
- The possible power of an inverted change in the base upon which the revaluation has been done. For example: The possible power of a decrease in the CPI in the first half of the coming year may be smaller than the possible power of a decrease in the US Dollar rate in the same period; or: The possible power of a general rise in the real estate prices in the next year many be bigger than the possible power of a rise in the fair value of the stock of a certain company in the real estate sector at the same period.

I. The sum of the dividend actually paid out has to be smaller than the sum received after using the above considerations, if the later sum includes profits of held companies, which have not yet been paid out and for which there is no obligation or a clear plan to pay them out in a short while (not more than 3 months).

J. The guiding principle is that as less certain it is that the held companies will pay out the said profit in a short while, the more the certain it is that the dividend payout should be smaller.

K. The sum of the dividend actually paid out has to be smaller than the sum received after using the above considerations, if there is a concern that the cash remained in the hands of the paying out company will not be sufficient considering its business plans for the next two years.

L. The guiding principle is that the less firmly formulated the business plans are, or as more they are based on unrealistic assumptions or if they are based on a leverage of an unclear availability or costs, the sum actually paid out has to be smaller.

10. Poison Pill

A poison pill is a generic name for a variety of means aiming to prevent takeovers of public companies[15]. Research shows that shareholders in a company usually profit from attempts to change the control and/or actual control struggles. In many cases, changing the control in a company contributes to the maximization of the company's value.

Supporting Mechanisms which do not Delay or Prevent Control Changes: We recommend supporting mechanisms which do not delay or prevent control changes. We believe that in cases of attempts to change the control in a public company, one has to take into account the wishes of all the shareholders and the market forces have to be allowed to act where the share price represents situations of under-management or default.

11. Settling and Liquidation Procedures due to failed Bonds

Our recommendation regarding settlings of debt is based on an economic analysis of the proposed settlement while clearly distinguishing between the interests of the bond holders and those of the shareholders.

When inspecting the settlement agreement we will address the following points in accordance with their relevance to the proposed settlement:

A. Inspecting the Settlement Agreement and the Alternatives: We will check the economic worthiness of the settlement agreement against possible alternatives, including the liquidation of the company. We will check the possibilities to get competing offers

[15] It is an agreement which will take effect when a certain shareholder purchases stock in the company to an extent which provides them a certain controlling ability (usually 15%-20%). In most cases the agreement includes allocation of shares by the Board of Directors in favor of existing shareholders, with a significant discount (can reach 50%). The poison pill mechanism has proven to be an effective defense tactic in the world. In Israel, in view of the control structure, this mechanism has not been tried yet and is not really common in public companies in Israel. One may assume it has succeeded in expelling unwanted takeovers.

from alternative controlling shareholders. The control will not remain in the hands of the current controlling shareholder, if it turns out that the situation of the bonds' holders will become better by an inflow of capital from an alternative controlling shareholder.

- In order for the controlling shareholder to stay in their position, they will have to put into the company and/or the bonds holders a value which will not be less than the value of the shares which will remain in the hands of the controlling shareholder plus the value of waiving the claims against them.
- Assessing the probability of the company's ability to abide by the proposed settlement agreement, will to a large extent be the deciding factor in regards to the value of the new inflow.
- We will check to see if the characteristics of the settlement reflect the risk level (interest, collaterals).
- We will inspect requests for partial inversions to shares, so that the bonds holders will be able to enjoy an improvement in the situation and rises in the shares price.
- We will investigate the extent of the involvement of additional debtors, including loaning banks and also that of controlling shareholders and/or potential investors.

B. Allocating Minimum Time for Holders to Make a Decision: In view of the multitude of settlements being formulated in the market, the bonds holders meetings are being called by the companies or by the trustees in such time schedules that do not allow reasonable time for proper consideration and decision making. Since the meeting is being called by a court order, there is a concern that if the meeting is not held in time, the company will be harmed. In reality, we see that the settlements take a long time and that the time factor is used mainly to produce pressure on the holders. Therefore, we will recommend that the holders vote against decisions in every bonds meeting in which the time allowed for decision making is less than 9 business days.

15. Warrants

We will review Changes in the terms of the warrants, while paying attention to their essence and their impact on the shares and options holders. Our recommendation on these subjects will take into account the fact there may be changes which reflect a built-in conflict of interests between the option holders and the holders of other securities of the company.

16. Insurance, Indemnification and Exemption of Office Holders

In view of the current business reality, we believe that the company should be allowed to take measures in order to protect the office holders and allow them appropriate space to make decisions involving calculated risks taking, when they act with good will and with prudence. The adoption of the regulations dealing with these subjects will be done in accordance with the instructions of the Companies Law. We will check to see if the suggested arrangements include exceptional instructions.

A. **An Engagement with Insurance Coverage** – We believe that office holders in the company should be covered by insurance, since this is the initial layer in which the company wishes to disperse its risks. In such an engagement we will check to see if the paid premium is reasonable in relation to insurance coverage.

B. **Indemnification**[16] - We believe that the indemnification sum should be limited to the financial capability of the company at the time the indemnification is granted. by common practice the maximum indemnification sum for all the office holders together, is limited to around 25% of the company's equity capital, with the exception of the minority's rights, at the time of the actual payment of the indemnification. In addition, the indemnification sum paid to the office holder will be according to the gap between the liability sum and the sum received under the insurance policy or another indemnification agreement in this matter. Such a limitation on the maximum indemnification payment has to be included in the company's articles.

C. **Exemption**[17] **-** We will support exempting all the office holders, including controlling shareholders and their relatives, provided that the articles and all the exemptions of the company to Directors and office holders will state that the granted exemption does not apply on a decision or a transaction that the controlling shareholder or any office holder in the company (including office holders other than the one receiving this exemption letter), have a personal interest in. This policy is subject to our discretion in each and every case. Among other things, we will oppose provision of exemptions even in the above circumstances, if a court has in the last there years approved the submission of a class act or derivative actions, as the case may be, against the controlling shareholder in

[16] This is actually an "internal insurance coverage" of the company towards its office holder in regards to liabilities they form towards third parties.

[17] Since the issue here is the relationship between the company and the office holder, then the meaning of the exemption is that the company will not prosecute the office holder in case they have breached their loyalty obligations towards it, it will not see them as being responsible for the damage and will not act against them.

the company or against office holders in it, which deal with breaching the fairness obligation, loyalty obligation or committing discrimination against minority shareholders.

17.Appointing an a Auditing CPA

Aspects of Reviewing the Appointment of a CPA to be the Auditor: We will recommend that the general meeting checks the appointment of the auditing CPA, while addressing the following aspects:

- Capability and professionalism.
- Independence and lack of conflicts of interests between their job as a CPA auditing the company and other connections they may have with shareholders/office holders.
- Size of their wages.
- The ratio of the fees for their auditing and tax services against the payments for other services, while checking the nature of the other services.

  We will recommend opposing the appointment of an auditing CPA, if the extent of their costs for auditing and tax services in the preceding year to the date of their appointment was lower than 70% of the size of the total fees paid to them.
- In the last three years, has the company been obliged to present anew its financial statements, among other things, due to mistakes or essential deviations in regards to estimations or assumptions.
- In the last years, has the court approved a class act or a derivative action against the CPA auditing the company.

18. Retroactive Approval of Transactions

A. **Approving Transaction in a Non-Appropriate Process**: We will recommend opposing retroactive approvals of transactions or agreements which have been approved in a non-appropriate process in the past and being brought after the fact for the approval of the general meeting**,** except in cases where the request is on behalf of a court and after a settlement agreement has been submitted by the parties**.**

B. **Approving the Terms of Service and Occupation of a CEO or Director:** In the matter of approving service and occupation terms of a CEO or a Director, we will not be against acceptance of an approval of the general meeting in the next annual meeting of the company, but only pending that the Remuneration Committee and the Board of Directors had approved the terms of service and occupation, that the service and occupation terms

abide by the remuneration policy and that the service and occupation terms are not better or significantly differ from the past[18]. In addition, Entropy has not been against similar service and occupation terms in the past.

19. Changes in the Articles of a Company and in the Reporting Format

The requested changes in the articles will be reviewed while addressing their nature and essentiality as well as the way in which they abide by the wording and the requirements of the law. Generally, we will review the wording of the articles and check to see if the changes being performed may harm the minority shareholders.

Following are several essential reservations:

A. **Decreasing the Required Majority**: In a general and sweeping way, we have reservations regarding amendments meant to decrease a majority required in approving essential matters in general meetings (i.e. decisions regarding capital changes, decisions regarding essential processes such as mergers, changes to the articles).
B. **Unreasonable Time Limits**: We will have reservations to instructions in the articles which allow calling general meetings with unreasonable time limitations, which may prevent the shareholders from having an exhaustive dialog with the company's representatives on the issues of the meeting.
C. **Sole Discretion in Dividend Pay-Outs**: We will recommend opposing an amendment which allows the Board of Directors sole discretion in the matters of dividend payouts. This is a very important decision for the shareholders, as specified in section 9 above and it is appropriate for it to be brought to the inspection of the shareholders in a special majority.
D. **The Version of the Companies Law in Regards to Indemnification and exemptions**: We have reservations to the wording of the Companies Law in regards to the subject of Indemnification (section 260 B1A), because it does not set quantitative parameters to its size and also gives the Board of Directors sole discretion in setting the size of the remuneration. We believe that the indemnification sum allowed in the articles and in the indemnification letter should be limited, in accordance with the financial capability of the company at the time of the indemnification and also to exclude the exemption granted to the controlling shareholder in regards to decisions or transactions in which they have any personal interest in, as detailed in section 16 above.

[18] The Companies Regulations (reliefs in transactions with stakeholders)(amendment 2) 5776-2016.

E. **Appointing a Director by the Board of the Directors**: We will recommend allowing the appointment of a Director by the Board of Director, only as long as the appointment is submitted for the approval of the general meeting up to 6 months after the fact. The service of such a Director will be valid only until the next meeting.

F. **Level of Reporting in Transitioning to Dual Listing**: When changing the listing format in the transition to dual listing (transitioning from reporting according to the requirements of chapter F of the Securities Law to reporting according to the requirements of chapter E 3 of the Securities Law), and in order to avoid any damages to the investors, we will check to see whether the change in the format of the reporting is expected to negatively affect the level of information and transparency the investors had been used to and if essential issues for the investors are omitted from the annual reports of the foreign companies, that enjoy reliefs in the reporting requirements.

   The reports upon which the law of dual listing applies, following which these companies are entitled to reliefs in the reporting are: (A) The 20-F reports, which is the annual report, (B) The 6-K report, which is a quarterly report. Against this, the reports submitted by the local companies in the Domestic US Companies, where one can find an extensive disclosure in format and the way they are presented are: The 10-K report (annual report) and the 10-Q (quarterly report).

   In view of the above we will require that the level of disclosure and transparency be in the reporting format of the domestic US companies. The equalization to the reports submitted by the US domestic companies is meant to avoid harm to investors in the requirements regarding the level of disclosure, the transparency and the way of presentation.

G. **Stipulation to Israeli Law in Dual Listings**: In the process of formulating our recommendation while in the process of transitioning to dual listing we will check the need to include in the prospectus a stipulation that the Israeli Law and the authority of the Israeli courts will apply on the Israeli shareholders in all cases even after the transition.

20. Administrative Issues

A. In the framework of the ongoing management of the company's business, managerial ongoing decisions are being made, that sometimes require the approval of all the shareholders. We check every such matter as the case may require, while paying special attention to the business results of the suggested process on the good of the company in the mid-long term. Examples to such decisions on administrative issues are: changing the name of the company, allocating funds of the company to charity, etc.

B. In addition, we will ask and recommend adding a clause to the articles of the company, according to which the company will be required to include all the issues on the agenda of the general meeting in a voting document to be published by it.

C. A preliminary Discussion in General Meetings which have not yet Publicly Reported – In recent years, there is an increase in companies applying to Entropy prior to a formal report on calling the meeting and sometimes even before the issue has been brought up for discussion at the management and/or the Board of Directors. After frequent changes in the regulation, especially in issues where a special majority is required, and in view of our wish to provide an appropriate service and solutions to public companies, most of these service requests have been treated so far. However we believe that a preliminary discussion has negative effects on the ongoing work processes in the company and therefore a preliminary discussion may create discrimination among the companies, and may even cause the most optimal final outline to be biased from the point of view of the minority shareholders, including decreasing from the responsibility the Directors and managers in the companies. Therefore, in view of the multitude of cases and sensibility of the subject, we update our approach towards an approach similar to the common practice in similar international consulting firms, and state that a discussion in the subjects of the general meeting will be held only after the subjects of the meeting have been published.

D. Summoning Meetings in Extremely Busy Periods – Entropy deals with providing recommendations to dozens of thousands decisions in general meeting annually and in front of hundreds of issuers. In parallel, the institutional bodies are required to make decisions, according to Entropy's recommendation, under huge performance pressures, in a period of extreme workloads (such as the major holidays and year ends). We often find that many companies call several general meetings every year, in addition to the annual meeting, where every one of them deals with different subjects, sometimes stemming from current needs. The multitude of meeting per company, results in a situation in which all the system dealing with the relevant subjects works under pressure and does not utilize to its fullest the appropriate treatment professionally, economically and even from the corporate governance aspect. Reducing the number of meetings and their concentration to one meeting, would enable diverting more resources to the interface with the company and its representatives. After researching the subject in parallel countries in the world and in international companies like ISS, we found that the consulting firm (as well as the institutional bodies themselves) are guiding to reduce the number of meetings and concentrate them to one meeting and also not to call meetings in busy times such as at the

end of the year. That, in view of the fact that a multitude of meetings in a short while prevents the shareholders from best inspecting all the subjects on the agenda, especially when the subjects are dispersed among several meetings and may provide the shareholders with a non-complete picture. Also, the calling of several meetings a year costs the company a lot of money and requires significant administrative time from its managers and representatives.

Therefore, we will encourage the companies to concentrate the subjects and to call general and special meetings so that they will have one general meeting which concentrates all relevant issues, in a way similar to what is common in foreign companies. This subject will also influence the corporate governance evaluation of the companies.