Vanguard

Vanguard-advised funds

Proxy voting policy for Mexican portfolio companies

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Introduction

The information below, organized according to Vanguard Investment Stewardship's four pillars of corporate governance, is the voting policy adopted by the Boards of Trustees of the Vanguard-advised funds (the "Funds' Boards") and describes the general positions of the funds on proxy proposals that may be subject to a shareholder vote at Mexico-domiciled companies.[1]

It is important to note that proposals often require a facts-and-circumstances analysis based on an expansive set of factors. Proposals are voted on case by case, under the supervision of the Investment Stewardship Oversight Committee and at the direction of the relevant Fund's Board. Companies should abide by the relevant local laws and regulations of the market in which they are listed and follow any applicable local corporate governance codes and best practices.

These local corporate governance codes form the basis of the funds' country-specific guidelines. However, they may differ and, in some cases, require a higher level of governance best practice than the local corporate governance code.

Timely and relevant public disclosure is key to the implementation of our voting policies. The funds can only factor certain information into voting decisions when it is publicly disclosed in a timely manner prior to proxy voting deadlines. As such, the funds generally do not support proposals for which disclosure is insufficient to enable an informed vote.

The following policies are applied over an extended period of time; as such, if a company's board is not responsive to voting results on certain matters, a fund may withhold support for those and other matters in the future. Regardless of whether proposals are submitted by company management or by other shareholders, they are voted in accordance with these policies and as determined to be in the best interests of each fund, consistent with its investment objective.

1 Vanguard's Investment Stewardship program is responsible for proxy voting and engagement on behalf of the quantitative and index equity portfolios advised by Vanguard (together, "Vanguard-advised funds"). Vanguard's externally managed portfolios are managed by unaffiliated third-party investment advisors, and proxy voting and engagement for those portfolios are conducted by their respective advisors. As such, throughout this document, "we" and "the funds" are used to refer to Vanguard's Investment Stewardship program and Vanguard-advised funds, respectively.

Pillar I: Board composition and effectiveness

In the interest of maximizing the long-term return of their investment in each company, the funds seek to ensure that the individuals who serve as board directors to represent the interests of all shareholders are appropriately independent, experienced, committed, capable, and diverse. Diversity of thought, background, and experience, as well as personal characteristics (such as gender, race, ethnicity, and age), meaningfully contributes to the ability of boards to serve as effective, engaged stewards of shareholders' interests.

In order to appropriately represent shareholder interests in the oversight of company management, at least 25% of directors should be independent, as should all of the members of the board's audit committee and corporate governance committee (for noncontrolled companies).[2] While the funds generally rely upon the relevant exchange listing or regulatory requirements in establishing a director's independence, there may be instances (such as former CEOs) in which directors who may be "technically independent" are considered otherwise after engagement and/or research.[3]

As detailed below, if a board's or committee's composition is inconsistent with these independence standards, a fund may not support (a) the nonindependent nominees on the board/committee and (b) members of the nominating/governance committee on the ballot.

Board independence

Independence is defined in accordance with local regulations and best practice standards, and therefore, a fund will generally defer to these standards in assessing director independence (including the boards' affirmative determination of a director's independence under those standards). The exception to this rule is that former CEOs will never be considered independent unless they only held an "interim" CEO position for less than 18 months. An interim CEO who held that temporary position for less than 18 months will be considered independent three years after leaving the position.

A fund will generally vote against the nonindependent board members of a company, or the proposed slate of directors (if directors are elected as a slate) of a company, that does not maintain a board that is composed of at least 25% independent directors. In addition, a fund will generally vote against directors, or a proposed slate of directors (if directors are elected as a slate), whose names and biographical details have not been publicly disclosed sufficiently in advance of the company's general meeting.

The funds will look for boards of widely held, noncontrolled companies to make progress toward having a majority independent board in alignment with global best practice standards, or at least to maintain a level of board independence proportionate to, and reflective of, the company's ownership structure.

Key committee independence

A fund will typically vote against nonindependent directors who serve on the audit committee or on the corporate governance committee at noncontrolled companies, and nonindependent directors who serve on the corporate governance committee at controlled companies when such committee is not composed of a majority of independent directors.

2 The funds will look for the majority of corporate governance committee members to be independent at controlled companies (those in which a majority voting interest is held by company insiders or affiliates).

3 For example, a fund will generally consider former CEOs of the company—other than those who may have served in an interim capacity for less than 18 months—as permanently nonindependent members of their board. In addition, CEOs who serve on one another's boards (so-called interlocking directorships) may also be considered nonindependent.

The funds look for boards to make progress toward having key committees (that is, audit, compensation, and nomination committees) that are composed entirely of independent directors in alignment with global best practice standards.

Director attendance

A fund may vote against directors who attended less than 70% of board or committee meetings (in the aggregate) in the previous year unless acceptable, extenuating circumstances are disclosed or they have served on the board for less than one year.

Director capacity and commitment

Directors' responsibilities are complex and time-consuming. Therefore, the funds seek to understand whether the number of directorship positions held by a director makes it challenging to dedicate the requisite time and attention to effectively fulfill their responsibilities at each company (sometimes referred to as being "overboarded"). While no two boards are identical and time commitments may vary, the funds believe that limitations on the number of board positions held by individual directors are appropriate, absent compelling evidence to the contrary. A fund will vote case by case on director elections when the number of directorship positions a person has accepted makes it challenging to dedicate the requisite time and attention to effectively fulfill their responsibilities at a given company.

The funds look for portfolio companies to adopt good governance practices regarding director commitments, including an overboarding policy and disclosure of the board's oversight of the implementation of that policy. Helpful disclosure includes a discussion of the company's policy (e.g., what limits are in place) and, if a nominee for director is in conflict with that policy, any considerations and rationale for their nomination. Additionally, it is good practice to include disclosure of how the board developed its policy and how frequently the policy is reviewed to ensure it remains appropriate.

Board composition

The funds look for boards to be "fit for purpose" by reflecting appropriate diversity of skills, experience, perspective, and personal characteristics (such as gender, age, race, and ethnicity) resulting in cognitive diversity that enables effective, independent oversight on behalf of all shareholders. The funds believe that the appropriate mix of skills, experience, and characteristics is unique to each board and should reflect expertise related to the company's strategy and material risks from a variety of vantage points.

The funds look for companies to disclose their perspectives on the appropriate board structure and composition for their company and how those elements support the company's strategy, long-term performance, and shareholder returns. Disclosure of how the board's composition evolves over time enables shareholders to better understand how the board is positioned to serve as effective, engaged stewards of shareholders' interests.

The funds look for disclosure of tenure, skills, and experience at the director level (sometimes referred to as a "skills matrix"). To this end, a fund may support requests for disclosure of the company's approach to board composition, inclusive of board diversity. A fund may also support the company's adoption of targets or goals related to board diversity. The funds will not prescribe what such targets should be, unless otherwise specified by applicable laws, regulatory requirements, or listing standards.

To evaluate board composition in relation to this policy, factors for the funds to consider include applicable market regulations and practices, along with additional company-specific context.

- Boards should reflect diversity of attributes including tenure, skills, and experience.

- A board should also, at a minimum, represent diversity of personal characteristics, inclusive of at least diversity in gender, race, and ethnicity on the board.
- Boards should take action to reflect a board composition that is appropriately representative, relative to their markets and to the needs of their long-term strategies.
- Disclosure of directors' personal characteristics (such as race and ethnicity) should occur on a self-identified basis and may occur on an aggregate level or individual director level. The funds look for disclosure of skills and experience at the director level.
- Companies should provide disclosure regarding their process for evaluating the composition and effectiveness of their board on a regular basis, the identification of gaps and opportunities to be addressed through board refreshment and evolution, and a robust nomination (and renomination) process to ensure the right mix of skills, experience, perspective, and personal characteristics into the future.

Absent a compelling reason, a fund will vote case by case on the nomination committee chair (or any other relevant director) if a company's board is not taking action to achieve board composition that is appropriately representative relative to market norms, local regulatory or listing standards, and the needs of the company's long-term strategies.

Escalation process: Director and committee accountability

Directors are generally nominated by boards and elected by shareholders to represent their interests. While a fund may generally support the board's director nominees, if there are instances in which the board has failed to respond to actions approved by a majority of shareholders, unilaterally taken action against shareholder interests, or, in the fund's view, failed in its oversight role, the fund may withhold support from those directors deemed responsible (generally based on their functional or committee-level responsibilities.

Contested director elections

A fund will vote on shareholder nominees case by case in contested director elections. The analysis of proxy contests focuses on three key areas:

- *The economic and strategic case for change at the target company*
  - How has the company performed relative to its peers?
  - Has the current board's oversight of company strategy or execution been deficient?
  - Is the dissident focused on strengthening the target company's long-term strategy and shareholder returns?
- *The quality of company governance*
  - Did the board engage in productive dialogue with the dissident?
  - Is there evidence of effective, shareholder-friendly governance practices at the company?
  - Has the board actively engaged with shareholders in the past?
- *The quality of the company and dissident board nominees*
  - Are there concerns with the independence, engagement, or effectiveness of the incumbent board?
  - Has the board delivered strong oversight processes with long-term shareholders' interests in focus?

— Are the directors proposed by the dissident (whether the full slate or a subset) well-suited to address the company's needs, and is this a stronger alternative to the current board?

Discharge of directors and/or management

Generally, a fund will vote for proposals to discharge the board, individual directors, and/or management in the absence of concerns regarding a lack of oversight, legal proceedings, or other egregious governance issues.

Pillar II: Board oversight of strategy and risk

Boards are responsible for effective oversight and governance of their companies' most relevant and material risks and for governance of their companies' long-term strategy. Boards should take a thorough, integrated, thoughtful approach to identifying, quantifying, mitigating, and disclosing risks that have the potential to affect shareholder value over the long term. Boards should communicate their approach to risk oversight to shareholders through their normal course of business.

Capital structures

- *Dividends.* A fund will generally vote for proposals to allow a dividend equal to 5% of a company's net income from the previous fiscal year for preferred shareholders.
- *Share issuance requests.* A fund will consider total dilution to existing shareholders and the company's history of issuing capital. A fund will generally vote for share issuance requests with preemptive rights up to 100% of currently issued capital.
  - A fund will generally vote for share issuance requests without preemptive rights up to 20% of currently issued capital.
  - A fund will generally vote case by case on proposals to create/amend/issue preferred stock, taking into account the reason for the issuance, the ownership profile of the company, any historical abuses of share issuances, and the company's general approach to shareholder rights.
- *Debt issuance.* A fund will vote case by case on proposals to issue debt and/or restructure debt, taking into account:
  - Any convertible features and the potential effect on dilution;
  - The company's financial position; and
  - The company's ability to take on the proposed debt.
- *Share repurchase.* A fund will vote for proposals to provide companies the authority to repurchase shares so long as the repurchase complies with Mexican law.
- *Reduction of capital/cancellation of shares.* A fund will typically vote for proposals to reduce the outstanding share capital or cancel treasury shares, so long as the terms are in the best interests of shareholders.

Independent auditors

Auditor appointment and auditor's fees. A fund will generally vote against the appointment of the auditor and setting the auditor's fees in instances where tax and all other fees exceed the audit and audit-related fees and/or exceed a reasonable amount, unless the company's disclosure makes it clear that the nonaudit fees are for services that do not impair independence and/or the imbalance was due to an event that was transactional and one-off.

A fund will vote case by case on the auditor's appointment/reappointment when there is a material misstatement of financials or other significant concern regarding the integrity of the company's financial statements.

A fund will generally vote for the appointment of a new auditor unless there is a compelling reason why the new auditor selected by the board should not be endorsed.

A fund will generally vote against proposals to indemnify the auditor, and will vote case by case on any proposal to limit an external auditor's liability, taking into account the explanation provided by the company for such liability limitation.

Mergers, acquisitions, and financial transactions

The funds seek to assess the likelihood that a transaction preserves or will create long-term value for shareholders. A fund will vote case by case on all mergers, acquisitions, and financial transactions based on a governance-centric evaluation focused on four key areas:

- Valuation
- Strategic rationale
- Board oversight of the deal process
- The surviving entity's governance profile

In evaluating board oversight, the fund will consider independence, potential conflicts of interest, and management incentives.

Environmental/social proposals

A fund will vote case by case on all shareholder proposals, including proposals that focus on environmental and social issues, such as requests of disclosures, setting of targets or goals, and adoption of policies and practices.

Clear, comparable, consistent, and accurate disclosure enables shareholders to understand the strength of a board's risk oversight. Because sustainability disclosure is an evolving and complex topic, a fund's analysis of related proposals aims to strike a balance between avoiding prescriptiveness and providing a long-term perspective.

Each proposal will be evaluated on its merits, with particular attention to the wording of the proposal, and in the context that a company's board has ultimate responsibility for providing effective ongoing oversight of strategy. This includes sector- and company-specific sustainability risks and opportunities that have a demonstrable link to long-term shareholder value.

A fund may support a shareholder proposal that:

- Addresses a shortcoming in the company's current disclosure relative to market norms;
- Reflects an industry-specific, materiality-driven approach; and
- Is not overly prescriptive about time frame, cost, or other matters.

Pillar III: Executive pay (compensation)

Compensation policies policies linked to long-term relative performance are fundamental drivers of sustainable, long-term returns for a company's investors. Providing effective disclosure of compensation policies, their alignment with company performance, and their outcomes is crucial to giving shareholders confidence in the link between executives' incentives and rewards and the creation of long-term value for shareholders.

Advisory votes on executive compensation

Because norms and practices vary by industry type, company size, company age, and geographic location, the following guidelines illustrate elements of effective executive compensation plans and are not a "one-size-fits-all" tool.

A fund's considerations when evaluating executive pay fall into three broad categories:

- *Alignment of pay and performance.* The funds look for evidence of clear alignment between pay outcomes and company performance. This is mainly assessed through alignment of incentive targets with corporate strategy and analysis of three-year total shareholder return and realized pay over the same period versus a relevant set of peer companies. If there are concerns that pay and performance are not aligned, a fund may vote against a pay-related proposal.
- *Compensation plan structure.* Plan structures should be aligned with the company's stated long-term strategy and should support pay-for-performance alignment. Where a plan includes structural issues that the funds determine have led to, or could in the future lead to, pay-for-performance misalignment, a fund may vote against a pay-related proposal. For compensation structures that are not typical of a market, the funds look for specific disclosure demonstrating how the structure supports long-term value creation for shareholders.
- *Governance of compensation plans*. The funds look for boards to have a clear strategy and philosophy on executive pay, to have robust processes to evaluate and evolve executive pay plans, and to implement executive pay plans responsive to shareholder feedback over time. The funds also look for boards to communicate these matters via company disclosures. Where pay-related proposals consistently receive low support, the funds look for boards to demonstrate responsiveness to shareholder concerns.

Generally, a fund will vote case by case on all compensation proposals and will support those that enhance long-term shareholder value. It may also vote for compensation proposals that reflect improvements in practices, even if the proposals are not perfectly aligned with these guidelines but are clearly in the interests of long-term shareholder value.

A fund will generally vote against compensation proposals when the details of a company's compensation policy are not disclosed to shareholders. The funds look for companies to provide robust disclosure of an overall remuneration policy for executives that includes a robust narrative and cohesive assessments of executive pay packages, including an overview of the weighting, structure, and performance alignment for all relevant incentive plans.

Equity compensation plans

A fund will vote case by case on equity compensation plans for employees. In general, a fund will support the adoption of equity-based compensation plans if the potential dilution (from all plans) is 5% of issued capital or below for a mature company, and 10% of issued capital or below for a growth company.

In general, a fund will vote against the approval of plans if:

- The potential dilution exceeds 5% of issued share capital for a mature company or 10% of issued share capital for a growth company;
- The plan allows for options to be issued at a discount to fair market value; or
- The information disclosed is not sufficient to determine the two above points.

Nonexecutive director compensation

In general, a fund will vote for nonexecutive director fees that seem reasonable, are in line with peers, and take into account the amount of time required of the nonexecutive directors to fulfill their roles.

A fund will generally vote against the approval of any nonexecutive director fees in the absence of sufficient disclosure to determine the reasonableness of such compensation.

Pillar IV: Shareholder rights

The funds believe that effective corporate governance includes shareholders having the ability—in proportion to their economic ownership of a company's shares—to effect and approve changes in corporate governance practices and the composition of the board. The funds look for companies to adopt governance practices that support board and management service in the interest of the shareholders they represent. Such governance practices safeguard and support foundational rights for shareholders. Proposals on many of the following matters may be submitted by either company management or shareholders; a fund may generally support proposals—irrespective of the proponent—that seek approval for governance structures that safeguard shareholder rights (and oppose those that do not) as described below.

Annual reports and accounts

A fund will generally vote for the approval of annual reports and accounts unless there is evidence of a particularly egregious reason not to support management's proposal or there are concerns about the integrity of the financial statements.

A fund will generally vote against the approval of annual reports and accounts if the audited financial statements have not been made available in a timely manner in advance of the voting deadline.

Board structure

A fund will vote for management and will vote case by case on shareholder proposals to declassify the board, and will vote against proposals to classify the board.

Additional share classes

This policy applies when a company issues more than one class of stock, with different classes carrying different voting rights. The funds' approach to this issue is principled yet practical. The funds remain philosophically aligned to "one-share, one-vote" approach, but are also mindful of the need not to hinder public capital formation in the equity markets. To that end, alignment of voting and economic interests is a foundation of good governance. This approach supports the idea of a newly public, dual-class company adopting a sunset provision that would move the company toward a one-share, one-vote structure over time. A fund will vote case by case on proposals relating to the introduction of additional share classes with differential voting rights.

Reincorporation/change of domicile

A fund will vote case by case on proposals to reincorporate to another country and/or proposals for companies to change their primary listing.

A fund will consider the reasons for the relocation, including the company's history, the company's strategy, and the company's shareholder base, along with any differences in regulation, governance, and shareholder rights.

Amendments to articles of association

A fund will generally vote for minor amendments that include any administrative or housekeeping updates and corrections. When evaluating all other amendments to the articles of association, the following will be considered:

- Any changes to corporate law and/or listing rules that may require an amendment to the articles of association;
- Whether the amendments may result in corporate governance structures and/or processes that are not best practices or are a regression from what the company already does (taking into account any explanation provided by the company for the change); and/or
- Whether the amendments are detrimental to shareholder rights generally.

Change of company name

A fund generally will vote for proposals to change the corporate name, unless evidence shows that the change would negatively impact shareholder value.

Shareholder meeting rules and procedures

Quorum requirements. A fund will generally vote against proposals that would decrease quorum requirements for shareholder meetings below a majority of the shares outstanding, unless there are compelling arguments to support such a decrease.

Other such matters that may come before the meeting. A fund will generally vote against a proposal to approve "other such matters that may come before the meeting."

Adjournment of meeting to solicit more votes. In general, a fund will vote for the adjournment if the fund supports the proposal in question and against the adjournment if the fund does not support the proposal.

"Bundled" proposals. A fund will vote case by case on all bundled management proposals.

Change of date, time, or location of annual general meeting. A fund will typically vote for management proposals to change the date, time, or location of the annual meeting if the proposed changes are reasonable.

Hybrid/Virtual meetings. A fund will generally support proposals seeking to conduct "hybrid" meetings (in which shareholders can attend a physical meeting of the company in person or elect to participate online). A fund may vote for proposals to conduct "virtual-only" meetings (held entirely through online participation with no corresponding in-person meeting). Virtual meetings should not curtail rights—e.g., by limiting the ability for shareholders to ask questions.

A fund will consider support if:

- meeting procedures and requirements are disclosed ahead of the meeting;
- a formal process is in place to allow shareholders to submit questions to the board;
- real-time video footage is available, and attendees can call into the meeting or send a prerecorded message; and
- shareholder rights are not unreasonably curtailed.

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