COMMITTEE CORPORATE GOVERNANCE
PRIVATE FOUNDATION

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Response to the Green Paper on the EU corporate governance framework

The Belgian Corporate Governance Committee (the Committee) wishes to respond to two main questions of the Green Paper which it believes are of great importance for the basis for achieving an adequate corporate governance system and lie within the scope of the Committee.

The 'comply or explain framework' - Monitoring and implementation of Corporate Governance Codes

(24) Do you agree that companies departing from the recommendations of corporate governance codes should be required to provide detailed explanations for such departures and describe the alternative solutions adopted?

(25) Do you agree that monitoring bodies should be authorised to check the informative quality of the explanations in the corporate governance statements and require companies to complete the explanations where necessary? If yes, what exactly should be their role?

Preliminary remarks

The Committee would like to make two preliminary remarks to the green paper. First of all, the discussion on corporate governance has been constricted to a great extent. The discussion dangers to be held on three topics only: remuneration, risk and the supervisory function of boards. These topics are of great importance, but corporate governance comprises much more than these topics. Strategic direction, leadership and an appropriate allocation of capital are also of foremost importance. This should not be neglected.

Furthermore, the debate becomes more and more a legal discourse. Boards need to focus increasingly on compliance with rules and regulation to the detriment of behaviour. Many issues are discussed to adjust board structures but the quality of decision making, a critical point of view or the added value of a director is never

discussed. Structures are needed, and easier to regulate but will not give us the guarantee that companies will be better directed in the future.

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The ‘comply or explain’-principle

Firstly, the Committee would like to comment on the more general aspects and the system of the ‘comply or explain’ principle.

As mentioned in the RiskMetrics report, regulators, companies and investors support the ‘comply or explain’ approach. The Committee would like to underwrite this and is convinced the principle is a far better approach than regulation for introducing corporate governance standards. The comply or explain approach allows to take companies' individual circumstances into account. Next to this, the system also recognises differences between national legal and governance frameworks without interfering directly with one another in a counterproductive manner.

Nevertheless, the Committee recognises its shortcomings, as mentioned in the green paper, we realise that its effectiveness should be enhanced and that the principle should be strengthened.

A strong ‘comply or explain’ system is based on two expectations:

1. First of all adequate transparency requirements need to be in place to ensure informative disclosure.
2. Secondly, a mechanism needs to be in place to hold the boards of companies responsible for an adequate disclosure of its governance practices and, where appropriate, adequate explanations if such practices deviate from the recommended approach.

The Committee would like to underwrite the need for these two objectives as well as the need for a state of affairs of the measures already in place to strengthen the principle.

The Committee believes there is more time needed to support and implement existing measures and developments in the corporate governance framework. Priority should therefore be given to a full compliance with European Directives before developing new measures or impose new regulatory initiatives It is hard to judge the effectiveness of the system, given the time of implementation greatly differs in the different member states. Indeed, it took quite a long time before the European Directive on the corporate governance statement has been introduced into law in many member states (Greece has only developed its Code in March 2011).

In April 2010, the Belgian legislator implemented the European Directive 2006/46 on the Corporate Governance Statement. Although Belgium was a rather late adaptor we went much further by integrating into law quite a number of mere recommendations, especially regarding the remuneration of executives and non-executives in listed companies. Belgium certainly belongs to the few countries where these measures have been strongly implemented.

The so-called ‘gold-plating’, where the member states impose additional measures when implementing a directive, is also a danger lurking around the corner, which to a certain extent will bring competitive disadvantages in European and international standards to the surface.

A possible risk regarding legislation is that the Corporate Governance Codes become the victim of their own success. In those member states where the codes are applied well, it would not be reasonable to impose regulation. The Codes are set up and updated by governance experts who are well aware of the corporate governance context, its advantages and its shortcomings. The legislator looks at directives and measures from an entirely different perspective. The Committee strongly emphasizes the necessity for a flexible mechanism, where similar requirements can be differently implemented in line with cultural, legal and economic differences. Furthermore the Committee believes that European entrepreneurship is at risk with overwhelming attention of boards of listed companies for compliance and procedures at the detriment of involvement with strategy and business development.

Quality of the explanations

The Committee shares the European Commissions' opinion that improvement of the quality of the explanations given in the corporate governance statements are necessary. Where a company chooses to depart from a corporate governance code, the green paper mentions it should give "detailed, specific and concrete reasons for departure".

There is however, no common vision as to what constitutes an appropriate explanation. A few issues should be taken into consideration.

- The Committee believes the quality of the explanations should be enhanced.
- Departure from corporate governance codes should be supported and not be downturned, as the system is put in place to be able to adapt the measures to a company's specific characteristics.
- The Committee believes due care should be taken regarding the description of providing a good explain for departing from a corporate governance code. Detailed explanations are not always better and may pave the way for legal firms to come up with well thought over-the-top explanations to be legally covered against any shortcomings it may hold. The Committee is of the view that explanations must not be boilerplate, but would also like to stress the fact that the need for more detailed and founded explanations must neither become the reason for simply complying with a practice that does not fit the specific needs of the company.
- The Committee also underlines the responsibility of the boards in this respect to focus on the informative quality of the explanations and to decide whether the departure is chosen from a justifiable business perspective.
- The Committee would like to stress that focus on explanations is needed and finds it appropriate to disclose alternative solutions besides the companies' explanations in case such a solution is existent. Noticeably, this will not always be the case and should therefor only be taken up in the explanation when appropriate.

This taken into account, the Committee has planned to provide the Belgian listed companies with guidance on how to provide adequate explanations to the shareholders. The boards can certainly do more self-monitoring in this respect. Instruments for implementing corporate governance codes and measures are of high necessity and of great value to help listed companies to be aware of the framework and have a meaningful governance policy. Companies need to be encouraged in this respect, not regulated.

Monitoring corporate governance

In the first place, monitoring is the responsibility of the shareholders. They are the ones that should be engaged and encouraged and should have clear standards on how they should exercise this responsibility. Nevertheless, their monitoring is limited to the reporting quality of the information disclosed and should not be judged on the justification of the company's business perspective.

The Committee believes that already a certain amount of monitoring instances are in place. Monitoring bodies as stock exchanges, institutional shareholders, proxy voting agencies exist and play an effective role in monitoring the companies. Also private initiatives are in place for monitoring the application of the codes.

Belgium is a country where companies with controlling shareholdership is much more common than dispersed shareholdership. In this respect shareholders explaining are mainly written for themselves. Here the Committee does want to stress the important role of the independent directors to stand for the vision and protection of minority shareholders as well as the important "controlling" responsibility such (institutional) minority shareholders can carry out in this respect.

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