Federation of European Accountants
Fédération des Experts comptables Européens

22 July 2011

Commissioner Michel Barnier
European Commissioner for Internal Market and Services
European Commission
BERL 10/034
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Cc Claire Bury
Eric Ducoulombier
Nathalie de Basaldua
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Re: CLC/HBL/LAN/SHA

Dear Commissioner,

Re: European Commission Green Paper on the EU Corporate Governance Framework

FEE is pleased to provide you with its comments on the European Commission (EC) Green Paper on the EU Corporate Governance Framework.

Sound corporate governance is particularly important in financial reporting as it is a key factor in ensuring confidence in capital markets through the provision of financial and other information of the highest quality.

FEE commends the European Commission for its commitment to improve corporate governance in Europe for the benefit of all stakeholders and agrees that the main issues for this initiative are those identified by the Commission in this Green Paper, being boards, shareholders and the functioning of the "comply or explain" approach.

However, FEE believes that audit is such an important part of corporate governance for European entities that any improvements to corporate governance can only be considered when also giving due consideration to how the audit of the entity interacts with the other elements of the governance of the entity. Good corporate governance highlights the importance of non-executive directors and their structures and relationships with the board(s), including any board committees that the board may have established, such as the audit committee. It also focuses on internal controls, internal audit, external audit and disclosures about corporate governance, and in particular, the fundamental relationships and obligations between boards, auditors and shareholders. An important step in this regard was taken in 2006 in Europe by introducing the requirement for listed companies to publish a corporate governance statement which has clearly increased the focus on corporate governance. On a European Union level, the auditor is only required to check whether the corporate governance statement has been produced, but the current structure of laws, regulations and corporate governance codes differs significantly from one EU Member State to another. More involvement of the auditor could be envisaged to increase the degree of confidence of users in the corporate governance information. FEE analysed this further in its Discussion Paper on Assurance on Corporate Governance Statements[1] where we concluded that some information may be suitable for factual verification whilst other information may be subject to an assurance engagement. We refer to our Discussion Paper for a more detailed discussion of the matter.

Although not addressed in the Green Paper, the role of the audit committee could be further analysed, as there seems to be room for improvement of this particular part of the corporate governance of public interest entities including listed companies. Especially the relationship between the audit committee and the auditor is of key importance and improvements could be made at regulatory level as well as in the application of already existing requirements and guidelines to enhance the quality of the cooperation between the two parties.

The improvements needed could be with regard to clarifying the responsibility of audit committees vis-a-vis the board and also specifying in more detail what the monitoring responsibilities of the audit committee entail in practice. In some European Member States, audit committees are a new concept due to the transposition of the Statutory Audit Directive and these clarifications could facilitate a more consistent approach as to how audit committees discharge their duties in the various Member States. More consistency across the Member States could also facilitate the presence of non-national members in audit committees.

The Green Paper focuses on the composition and the competences of the board. Other aspects of boards are their role and responsibilities, which, except for the considerations regarding risk appetite and risk arrangements, are not touched upon in this Green Paper. The role and responsibility of the board is the cornerstone of good functioning of corporate governance, and is broader than merely aimed at risk appetite and risk management. The approach to these matters differs to some extent across Europe. Therefore, more could be done to encourage harmonisation and the exchange of good practices regarding the role of and functioning of boards across different companies and countries in addition to the responsibilities in relation to risk management and risk appetite.

[1] http://www.fee.be/fileupload/upload/DP%20Assurance%20on%20Corporate%20Governance%20Statements%200911%20Colour20112009541533.pdf

With regard to the specific issues raised in the Green Paper, our main comments can be summarised as follows:

1. Boards should collectively have the competences needed to discharge their duties which can be ensured by an appropriate composition that has sufficient diversity among the members. The diversity should be with regard to not only gender, but also background, age, ethnicity etc. The composition of boards should be based on the principle of "the best person for the job" which is not compatible with any kind of quotas which would therefore not be appropriate.
2. FEE fully supports the aim of engaging shareholders to a greater extent than is currently the case and believes that the appropriate approach will be to recognise that shareholders are not a homogenous group. Different measures may therefore be appropriate depending on which group of shareholders that is targeted and for which purposes.
3. FEE continues to support strongly the "comply or explain" principle as we believe that this principle remains appropriate as one of the cornerstones for the implementation of good corporate governance. However, some improvements as to how the principle is applied in practice could be introduced, especially with regard to the quality and content of the explanations. This could be done by setting clearer criteria in a proportionate reporting framework.
4. With regard to the scope of companies, sound and sustainable corporate governance is important for any company, regardless of its size and whether or not the company is a listed company. With this in mind, corporate governance measures should be proportionate to the nature, size and complexity of the entity and its business. Smaller companies should therefore be subject to proportionate requirements where relevant and to less stringent requirements than larger companies, as smaller unlisted companies are typically managed by their owners. They have fewer staff and engage with a smaller group of stakeholders (such as suppliers, customers and government agencies). Any policy actions envisaged in this area should therefore equally be proportionate with regard to size, complexity and number of shareholders of the entity. The main difference between listed and unlisted companies is the need for transparency to the public and towards its shareholders. The large differences in size and complexity within the group of unlisted companies should also be noted as they range from micro-entities to very large unlisted corporate companies.

FEE's ID number on the European Commission's Register of Interest Representatives is 4713568401-18.

For further information on this FEE[2] letter, please contact Hilde Blomme at +32 2 285 40 77 or via email at hilde.blomme@fee.be or Lotte Andersen at +32 2 285 40 80 or via email at lotte.andersen@fee.be from the FEE Secretariat.

Yours sincerely,

Philip Johnson
FEE President

[2] FEE is the Fédération des Experts comptables Européens (Federation of European Accountants). It represents 45 professional institutes of accountants and auditors from 33 European countries, including all of the 27 EU Member States. In representing the European accountancy profession, FEE recognises the public interest. It has a combined membership of more than 500.000 professional accountants, working in different capacities in public practice, small and big firms, government and education, who all contribute to a more efficient, transparent and sustainable European economy.

FEE's objectives are:

- To promote and advance the interests of the European accountancy profession in the broadest sense recognising the public interest in the work of the profession;
- To work towards the enhancement, harmonisation and liberalisation of the practice and regulation of accountancy, statutory audit and financial reporting in Europe in both the public and private sector, taking account of developments at a worldwide level and, where necessary, promoting and defending specific European interests;
- To promote co-operation among the professional accountancy bodies in Europe in relation to issues of common interest in both the public and private sector;
- To identify developments that may have an impact on the practice of accountancy, statutory audit and financial reporting at an early stage, to advise Member Bodies of such developments and, in conjunction with Member Bodies, to seek to influence the outcome;
- To be the sole representative and consultative organisation of the European accountancy profession in relation to the EU institutions;
- To represent the European accountancy profession at the international level.

Appendix: Responses to Questions

Corporate governance is of importance to all companies, although some measures may be more relevant for some companies and not for others. As a result, our views set out below are applicable for public interest entities, unless otherwise indicated.

General questions

Question 1: Should EU corporate governance measures take into account the size of listed companies? How? Should a differentiated and proportionate regime for small and medium-sized listed companies be established? If so, are there any appropriate definitions or thresholds? If so, please suggest ways of adapting them for SMEs where appropriate when answering the questions below.

Sound and sustainable corporate governance is important for any company, regardless of its size and whether or not the company is a listed company. However, corporate governance measures, although generally important, should be proportionate to the nature, size and complexity of the entity and its business and more comprehensive measures would be relevant in systemic companies, such as in financial institutions than in smaller companies. For the purpose of this question, in particular the last part of it, we focus on corporate governance for small listed companies. Although smaller listed and unlisted companies may be comparable in size and complexity of the business, it is important to distinguish between smaller listed companies and SMEs that are not listed companies for any policy measures in this area due to the difference in focus by stakeholders.

The Statutory Audit Directive already recognises a difference between large and small and medium-sized public interest entities for the establishment of audit committees, as the functions of the audit committee in small and medium-sized listed entities can be performed by the board under certain circumstances. The relationship between the audit committee and/or the board should still be recognised as an essential part of the corporate governance framework for the company. The regulatory measures applied for other corporate governance areas, besides in relation to audit committees, should be considered, as requirements could be relevant for some companies, whilst recommendations on corporate governance would suffice for other (smaller) companies.

There may be a concern that changes introducing important reductions are done with the only aim of reducing the costs for small listed companies. However, measures could have a significant impact on the level of competiveness, transparency and visibility which, in our view, would have an adverse impact on investors' interest in such companies. The views and needs of investors on this matter would therefore need to prevail and a balance needs to be struck between cost reductions and aiming at less administrative burdens over less transparency.

One way of employing a principles-based approach not to create additional costs for small listed companies, could be to focus on streamlining disclosures while maintaining a single level of regulation in the market for the benefits of investors ensuring the same level of transparency for all companies. In this exercise, we should guarantee an acceptable minimum level of regulation.

A potential definition for companies that would be subject to requirements for corporate governance would need to be carefully considered, as there is currently a variety of possible definitions. One definition that would be relevant would be the definition of public interest entities as defined in the Statutory Audit Directive with the embedded definition of small and medium-sized entities included. However, the transposition of the definition included in the Directive has resulted in significant differences at national level, and more could therefore be done in order to get a more consistent approach at European level as to what a public interest entity is.

Another possible definition of a small versus a large listed company would be the definition of a small listed company in the context of regular transparency requirements, as the one included in the amendment to the Prospectus Directive which states *“a proportionate disclosure regime … for the shares and offers by SMEs, and issuers with reduced market capitalisation*” and defines a small listed company as “ *'company with reduced market capitalisation' means a company listed on a regulated market and having had an average market capitalisation of less than EUR 100,000,000 on the basis of end-year quotes during the last three calendar years*".

In any case, we would strongly encourage the use of one single harmonised definition across the various European directives and regulations on what a public interest entity/listed entity is as well as what is to be understood under a small listed company, if such a category is further developed.

Question 2: Should any corporate governance measures be taken at EU level for unlisted companies? Should the EU focus on promoting development and application of voluntary codes for non-listed companies?

As already explained in further detail in our response to question 1, sound and sustainable corporate governance is important for any company, regardless of its size and whether or not the company is a listed company.

However, the attention for unlisted companies is significantly different compared to that for listed companies. This is already recognised in the Statutory Audit Directive and also in other areas of European legislation through the definition and specific additional requirements for public interest entities, for instance in relation to audit committees.

These requirements recognise the need for transparency to the public and towards its shareholders for listed companies which could be taken into account when considering any corporate governance *principles* for unlisted companies, reflecting the differences between listed and unlisted companies, also noting that there is large variety within the group of unlisted companies, ranging from micro-entities to very large corporate companies that are unlisted. Also, smaller unlisted companies are typically managed by their owners, they have fewer staff and engage with a smaller group of stakeholders (such as suppliers, customers and government agencies) and will therefore not have a need for extensive corporate governance principles compared to large unlisted multinational companies.

Some public interest entities as defined at national level that are unlisted, may find it useful to apply general corporate governance principles. However, to avoid that an unnecessary administrative burden is placed on unlisted companies in general, there does not seem to be a need for measures for promoting the development and application of corporate governance codes for other unlisted companies at European level at this point in time.

In this respect, also professional accountants have many competences which put them in a good position to significantly contribute to and add value to companies' corporate governance. Their expertise can be (and is) provided in a variety of ways, all subject to the relevant ethical and independence regulations and other requirements.

Boards of directors

Question 3: Should the EU seek to ensure that the functions and duties of the chairperson of the board of directors and the chief executive officer are clearly divided?

As mentioned with regard to financial institutions, all companies need able management to ensure good governance throughout the company. It is important to have an appropriate balance of power in any board system so that no single individual or group has unfettered control of the company.

It is essential that the principles of the roles of Chairman and Chief Executive should be performed by different people, balanced by a strong independent non-executive element in a system with a unitary board. In a two-tier structure, the management board and the supervisory board are already clearly divided and therefore fulfil the principle of division of duties. This approach is recommended in the 2005 Commission Recommendation on the role of non-executive or supervisory directors of listed companies and combined with the already recommended cooling off period for both unitary and dual systems, this recommendation remains appropriate for listed entities and other large unlisted public interest entities. As this issue relates to company law, it could be addressed as part of a wider analysis of that area.

Question 4:

a. **Should recruitment policies be more specific about the profile of directors, including the chairman, to ensure that they have the right skills and that the board is suitably diverse?**
b. **If so, how could that be best achieved and at what level of governance, i.e. at national, EU or international level?**

The trust that shareholders place in the board and in management can only be achieved if non-executive and supervisory directors are competent and have sufficient time to fulfil their role. Appropriate competences of board members and directors are highly relevant in any company and any board should include expertise in the specific industry and have an understanding of the wider macro economic consequences of a particular business model.

The key point is balancing skills and experience so that the company's board of directors *as a whole* has strong expertise relevant to the activities of the respective entity to be able to sufficiently challenge management in its discharge of duties.

Based on this, it would be more relevant to define the appropriate profile for the board as a whole and for its individual members, including the members of any board committees established by the board. For instance, it would be relevant for the board to clearly define the profile of the members of the audit committee given the need for specialised skills in accounting, auditing and other areas relevant to the company in question. Broader focus on profiles of members in recruitment policies would ensure the appropriate combination of the right skills and diversity of the board, given that board members are subject to induction programmes and continuous education in line with the 2005 EC Recommendation on non-executive directors.

The 2005 EC Recommendation on non-executive directors already includes some appropriate recommendations in the area related to competences of the board which remain relevant also when looking forward.

Question 5: Should listed companies be required to disclose whether they have a diversity policy and, if so, describe its objectives and main content and regularly report on progress?

Question 6: Should listed companies be required to ensure a better gender balance on boards? If so, how?

FEE supports diversity in companies as well as in the board of directors and its committees based on the overall principle of *"the best person for the job".* In this approach, due care should be given to the competences, qualifications and the collective responsibilities of the board of directors, whether or not this entails more differences in gender, background, age, ethnicity, etc. However, it is important to recruit from a sufficiently large and diversified pool of candidates, being substantially wider than an established network of candidates. A diversity policy describing these principles is bound to result in companies having more focus on diversity in general.

In FEE's opinion quotas of any kind for the members of the board would not be compatible with this overall principle as the primary criterium is that the competences of the board of directors collectively reflect the activities of the company.

The most important element, for the composition of the board and its committees, is ensuring that the board is run effectively, functions properly and works efficiently which comes down to a much broader aspect than merely the gender of the members, namely their backgrounds and expertise, similar to what is required for at least one member of the audit committee in line with the Statutory Audit Directive.

Transparency of these matters, including content of the policy and its effects, can only be supported and should be done, if the company has a diversity policy for the company as a whole and/or for the board and any relevant board committees. This would enable investors to include this issue in their investment decisions if the investors apply ethical criteria in their decisions. A disclosure requirement would therefore be most relevant for listed companies. Disclosures of a diversity policy and its application may also be information of importance to future employees in order to underline the culture of broad diversity within the culture of the company.

Question 7: Do you believe there should be a measure at EU level limiting the number of mandates a non-executive director may hold? If so, how should it be formulated?

Each director should be able to devote sufficient time and the necessary attention for each board on which the board member sits, also in times of crisis. This would be consistent with the 2005 EC Recommendation on the role of non-executive or supervisory directors in listed companies[3]. Directors in listed companies should be discouraged from accepting too many board appointments with due regard to their other duties and commitments to ensure that the ability to properly perform their duties is not compromised, having the overarching principle of having sufficient time in mind.

However, FEE considers that regulatory measures in the form of detailed rules at European level would not be appropriate. Instead, a comply or explain approach would be relevant to apply in this context, allowing shareholders to engage, if the board of directors do not devote sufficient time to the assignment given to them. EU Member States might decide to introduce specific rules on this issue, which is already the case in some national laws or corporate governance codes. FEE believes that having general principles at EU level, and leaving it to Member States to specify a particular limit, if they so wish, remains appropriate when looking forward.

Further details to complement the overarching principle could include:

- Requiring that the expected time commitment is clearly specified in the terms of reference for the board of directors, such as the number of meetings, expected contribution of each of the members, participation in committees, etc;
- Highlighting considerations related to proportionality, such as size and complexity of the company and the line of business it operates in;
- Setting specific expectations for directors' involvement in general and in times of crisis.

Board members in listed companies could be required to disclose board positions held in other companies by their non-executive or supervisory directors in line with current practice and as recommended in the EC Recommendation on the role of non-executive or supervisory directors in listed companies. Disclosures should include significant board or equivalent positions held in public sector or not-for-profit bodies.

[3] http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2005:052:0051:0063:EN:PDF

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Question 8: Should listed companies be encouraged to conduct an external evaluation regularly (e.g. every three years)? If so, how could this be done?

The EC Recommendation on the role of non-executive and supervisory directors in listed companies includes a number of relevant principles recommending a yearly self-assessment and evaluation of the (supervisory) board and also on transparency and communication recommending yearly disclosures on these matters. These principles still appear appropriate when looking forward.

In addition to the already recommended practices regarding self-assessment, FEE considers assessments *facilitated* by a party external to the board and to the entity appropriate. Such an externally *facilitated* assessment is likely to create more ownership of the assessment and its results compared to an evaluation of the board entirely carried out by an external evaluator. An externally *facilitated* assessment of the board would be appropriate for listed companies and should be carried out on a regular basis, but less frequent than annually, and whenever there is a significant change in the composition of the board of directors.

The following key characteristics of an external facilitator and the assessment that is facilitated could be considered:

- Evaluation of the performance of the board of directors as a whole and of its committees;
- The external facilitator should be independent, both of the board of directors and its committees, as well as of the company as a whole.

Question 9: Should disclosure of remuneration policy, the annual remuneration report (a report on how the remuneration policy was implemented in the past year) and individual remuneration of executive and non-executive directors be mandatory?

Question 10: Should it be mandatory to put the remuneration policy and the remuneration report to a vote by shareholders?

Major attention has been devoted to the consequences of the remuneration policies, especially in financial institutions. With regard to remuneration, it is important that attention is paid not only to the size of bonuses but also to the generation of sustainable value through realising the business strategy within preset and appropriate risk boundaries.

Where the board of directors plays a role in the remuneration process, this role should be performed in an objective and professional way. This is underlined in the EC Recommendations on the role of non-executive or supervisory directors in listed companies and on remuneration of directors in listed companies[4] by the recommended establishment of a remuneration committee.

A proper balance between regulation and recommendations would be needed, as only some aspects of remuneration, such as general remuneration policy principles, would be appropriate for regulation, and in this regard only for some companies, such as for listed companies.

[4] http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:120:0028:0031:EN:PDF

The main objective should be to have the principles set out in a remuneration policy and to ensure that these remuneration policies are transparent to all shareholders in listed companies. The disclosed information should lead to an understanding of how the long term goals of the strategy for the company are being achieved through the interaction between the remuneration policies for the individual executive and non-executive directors and the strategic goals for the company as a whole. In this context, active engagement of shareholders, in line with our comments to section 2 of this Green Paper should be considered which could be done by requiring shareholders to vote on remuneration policies.

Involvement of employees holding shares in the company has to be considered with caution as this could result in promotion of the self-interest of this particular group of stakeholders.

Question 11: Do you agree that the board should approve and take responsibility for the company's 'risk appetite' and report it meaningfully to shareholders? Should these disclosure arrangements also include relevant key societal risks?

The board of directors takes full responsibility for setting, updating, approving and monitoring the risk profile and strategy of the company and continues to be accountable for this key function which should include the general risk identification. In a two-tier system, the setting of the risk profile and strategy will be performed by the management board, whereas the role of the supervisory board is to approve and monitor the risk profile and strategy. The functions between the management board and the supervisory board are clearly divided and should not be mixed. Risk identification is more factual and would address the risks that may exist in relation to the business model and would also include the more judgemental commitment to risk appetite within the business model agreed. Any societal risks where the business model impacts the society and the environment, should be included in the board considerations. Disclosures of such information should be proportionate to the nature, size and complexity of the entity, and it should be clear from the disclosed information whether the societal risks are risks to the entity and/or to the society at large.

A significant amount of information on risk-related issues for companies is already available in the public domain, based on requirements in the Fourth Company Law Directive, and in IFRS, in particular in IAS 1 Presentation of Financial Statements and in IFRS 7 on Disclosures: Financial Instruments. Consideration should be given to the different needs of users of additional information on risk, which could be the board of directors, the supervisors or the public.

If there is scope for additional reporting on risk for companies, given the needs of investors in particular, proportionality of its possible content, level of detail, length, etc. of the information should be addressed. Suitable criteria for this additional risk information would be a prerequisite for consistent, relevant and useful information. These considerations would be most relevant for industries with high risk business models, such as financial institutions and less, considering the information on risk already made available, for other companies.

The level of involvement of the external auditors in relation to additional risk related information, if any, could be considered, giving due consideration to the extent of this involvement with the constraints to the independence of the auditor[5]. The level of involvement should be further analysed as the range of this involvement, based on a thorough cost-benefit analysis, could vary from no involvement at all to the auditor providing reasonable assurance on the content, if not already included in the financial statements and thus covered within the scope of the statutory audit[6].

Question 12: Do you agree that the board should ensure that the company's risk management arrangements are effective and commensurate with the company's risk profile?

Effective risk management arrangements that are aligned with the company's risk profile are a key part of good corporate governance and the board should commit to ensure that this is achieved in line with the requirements to do so in the European legislation. While retaining the responsibility for the determination of the risk management arrangements, this monitoring process by the board can and should to some extent be based on the work done by its committees, especially the audit committee and the risk committee, if such a committee has been established.

If requested by users, and although not aiming at providing assurance on the effectiveness of the companies' risk management arrangements, the involvement of the auditor could be further analysed as explained in further detail in our response to Question 11.

Shareholders

FEE has not responded to Questions 13-23 individually, but provides some general comments on shareholders below.

Regulation of shareholders' behaviour appears to be quite difficult in practice as shareholders usually use their rights to buy and sell shares whenever they consider it appropriate to optimise the return on their investment, also keeping the rules regarding insider trading in mind. Therefore, recommendations appear to be more feasible in this area and the principle of *"comply or explain"* may be the best approach in this context.

However, shareholders are not a homogenous group and the choice of approach would need to distinguish between controlling, significant interest, major holding (institutional) shareholders and small holding shareholders, as they have different investment strategies, roles and responsibilities.

[5] FEE recommends the adoption of the Independence Section of the International Ethics Standards Board of Accountants (IESBA) Code of Ethics for all entities.
[6] FEE supports fully the adoption of ISAs for all statutory audits in the EU through a legally binding instrument at EU level.

The general approach should be *"active engagement of shareholders"* and it could be worthwhile underlining the basic principle that when shareholders acquire shares, they obtain rights but also certain obligations as is the case with every asset. The aim should be to promote transparency, such as for investment policies and for structure of voting as well as through initiatives such as internet voting and the use of other IT technology.

It appears not to be feasible to require active engagement of all shareholders, regardless of their size and involvement with the company. A proportionate approach should therefore be used.

In particular, the shareholder's structure of the listed company should be transparent and this principle should be supported. The overall principle is active engagement of shareholders, which can only be done if the company is aware of the identity of its shareholders. The company should also keep in mind that minority shareholders are important for the overall governance of the company and due consideration should be given to the role that this group of shareholders play in the general governance structure of the company.

With regard to proxy voting, it may be worthwhile to more clearly identify the profile of who can act on proxy, as in some instances, proxy managers and proxy advisors are seen as similar to auditors, which in practice is not to be the case, given the independence requirements that auditors are subject to.

Monitoring and implementation of Corporate Governance Codes

Question 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?

FEE has, along with most other stakeholders, been a long standing supporter of setting robust, high quality principles and benchmarks for corporate governance at European level that should be applied using the '*comply or explain'* approach for all companies.

Although the *'comply or explain'* approach, in light of the financial crisis, has been criticised, FEE remains a strong supporter of the principle itself and believes that it remains appropriate for influencing the culture and behaviour in companies also when looking forward. In our view, this is and continues to be a preferable approach over laws and regulations in the area of corporate governance.

Application of the comply or explain principle should generally lead to "*comply*" as the cornerstone of the principle is to be more appropriately and widely applied by companies than providing low quality explanations for extensive deviations from a corporate governance code. As further discussed in our response to Question 25, the monitoring of the application could also contribute to enhanced quality in practice. Due care should be given to the impact on small and medium-sized companies in order to incorporate a proportionate approach for the application of the comply or explain principle.

In this context, there may be room for some clarification by setting clearer criteria through a reporting framework. This would facilitate a more consistent application of the comply or explain principle aiming at more comprehensive and qualitative explanations, as FEE, along with the Commission as referred to in the Green Paper, takes note of the criticism of the application, which relates especially to the quality of the explanations given and less on the "comply" part of the principle.

The clarification of the principle could be with regard to the content of the explanations. The explanation should contain adequate information regarding the areas where the corporate governance code has not been implemented, the reasons for the non-compliance and what alternative solution has been applied instead, where relevant. This is similar to the approach taken in the Swedish corporate governance code, as referred to in the Green Paper, and appears to be a measure that could facilitate a more consistent application with more informative explanations of non-compliance. Such more clear princples for the explanations could also to some extent mitigate the risks of explanations being articulated in generic boiler-plate disclosures as they would be more company specific.

The current structure of laws, regulations and corporate governance codes differ significantly from one EU Member State to another and although national differences should be taken into account, more could be done in finding common European solutions leading to a more consistent application of the comply or explain principle by the various European companies.

Question 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?

FEE agrees that the monitoring of the application of the comply or explain principle could be further enhanced, which as noted in the Green Paper would facilitate a more consistent application leading to higher quality in the explanations given. Transparency with regard to best practice examples of explanations given would also contribute to increasing the quality of the explanations.

The preparation and presentation of corporate governance reporting and statements is a responsibility of management and the board(s) of the company. The additional monitoring of such statements could be done by external parties and/or internal parties.

The external parties can be an auditor or the regulator. The auditor can add value by reporting on an independent assessment of whether certain aspects of the corporate governance statement comply with defined criteria and reporting standards in addition to providing verification of its existence, as required in the Fourth Company Law Directive. This involvement can increase the degree of confidence of users of corporate governance information. FEE has already in its 2009 Discussion Paper analysed the involvement of the auditor with regard to assurance on corporate

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governance statements[7]. We concluded that some information may be suitable only for factual verification in the corporate governance statement because it is subjective in nature. In such a case, auditors can check underlying facts on for instance remuneration of directors but will not be able to form an opinion as to whether a company's remuneration policy will lead to the directors achieving the company's stated strategy. Other information may be the subject of an assurance engagement, but the level of costs and benefits varies significantly. For example, providing assurance on a description of internal control may not require much time to be spent by the auditor, whereas forming an opinion as to the effectiveness of the internal control requires significantly more resources. Some information may even be too subjective for the auditor to be involved, such as whether the board is collectively effective in their discharge of the responsibilities to meet the strategies of the company.

The role of supervisory authorities is different compared to the role of the auditor with regard to monitoring activities. The role of external auditors is related to reporting on individual companies whilst supervisory authorities are geared towards the market as a whole focusing on investor protection as well as to the supervision of individual companies. The focus of supervisory authorities is therefore wider compared to the scope of the work of external auditors as they perform the tasks of monitoring and enforcement of the individual companies differently compared to the work of the auditor when providing assurance on the information.

In this regard, supervisory authorities would be best placed to monitor results of the application of the comply or explain principle by highlighting best practice examples in comparative studies. As already seen in practice, this will contribute to increased focus on the quality of the explanations given for the benefits of the companies and their stakeholders. A fruitful exchange of information between auditors and regulators, as both parties are involved in the monitoring of the application of the principle, would be beneficial to both and could be further enhanced.

It could also be considered whether there is an extended role for audit committees as an internal part in the monitoring process. This could for instance be done by supplementing the already required monitoring responsibilities for internal control in the Statutory Audit Directive with the responsibility of monitoring the application of corporate governance codes and ensuring the quality of the explanations given for non-compliance.

In defining the additional measures needed to enhance the quality of the explanations, the target audience should be kept in mind, as some considerations may be most relevant for internal purposes through private reporting to the audit committee, for instance whilst other information would be most relevant for supervisors or as public information to shareholders and the public at large. When relevant criteria have been defined, as discussed in our response to Question 24 above, the additional auditor's involvement with and reporting on the corporate governance statement and comply or explain with corporate governance codes can be further developed.

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[7] FEE Discussion Paper on the Auditor's Role regarding providing Assurance on Corporate Governance Statements, November 2009
http://www.fee.be/fileupload/upload/DP%20Assurance%20on%20Corporate%20Governance%20Statements%200911%20Colour20112009541533.pdf. We refer to our Discussion Paper for more a detailed discussion of the matter.