



The Scientific Analysis of Some European Corporate Governance Standards After Financial Crisis – Case in Belgium and The Netherlands

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Abstract

After the recent global crisis, corporate scandals and bankruptcy in US and Europe, there is some certain evidence on weak auditing, risk management, accounting and audit system. This paper chooses a different analytical approach and among its aims is to give some systematic opinions on corporate governance criteria as a benchmark for stock markets.

Firstly, it classifies limited Western European representative corporate governance (CG) standards into groups: The Netherlands and Belgium latest CG principles covered in group 1 while it uses OECD and ICGN principles as reference. Secondly, it , through analysis, identifies differences and advantages between above set of standards which are and have been used as reference principles for many relevant organizations.

Third, it establishes a selected comparative set of standards for a typical Western European representative corporate governance system in accordance to international standards. Last but not least, this paper covers some ideas and policy suggestions.

Keywords: Corporate Governance Standards, Board Structure, Code Of Best Practice, Financial Crisis, Corporate Scandals, Market Manipulation, Internal Audit

1. Introduction

After corporate scandals happening during and after global monetary and financial crises, it is necessary to re-evaluate code of corporate governance. In reality, many nations re-issue their principles of corporate governance as guidelines for their market and companies. This paper selects an easy-reading writing style, and it finds out that there is still some academic words need to be explained in further.

The organization of paper contents is organized as following. As our previous series of paper, Research literature and theories are covered in the first two sessions. Next, it followed by introduction of our research methodology in session 3 (3rd). Continuously, session four (4) covers our familiar groups of empirical findings. And our conclusion and policy suggestion is covered in the fifth (5th) session. Before last, there are exhibit session which covers some

summary of this paper's analysis and comparison. And lastly, a glossary note is provided with information for reference and because of reducing repeating terminology.

2. Body of Manuscript

Research literature review

There are many and controversial opinions on corporate governance theories and practices. For example, Jensen and Meckling (1976) presented their conceptual agency theory on the separation of ownership and management. Belgian Code 2009 stated that corporate governance is a set of rules and behaviors which determine how companies are managed and controlled.

Besides, Thailand 2006 Code defines CG as a set of structures and processes of the relationship b.t a firm's board of directors, its MGT and its shareholders to boost the firm's competitiveness, growth and long-term shareholder value with taking into account the interests of other stakeholders. Malaysian Code on CG 2012 defines CG as the process and structure used to direct and manage the business and affairs of the company towards enhancing business prosperity and corporate accountability with the ultimate objective of realizing long-term shareholder value.

Additionally, Berger et al (2013) found out that during the financial crisis, bank defaults are strongly influenced by a bank's ownership structure.

Generally, CG refers to the set of systems, processes and structures in which the company is governed.

Because there are not many researches and surveys done in Western European region on CG, next, what is the limited comparative standardized set of so-called comparative Western European corporate governance standards?

Theory of Corporate Governance, Scandal and Market Manipulation

Theory of manipulation

Market manipulation covers errors in interfering the market operation and creates false information on price or market for a financial commodity such as stock.

Aggarwal and Wu (2003) suggested a strong role for government regulation to discourage manipulation while encouraging greater competition for information. And more illiquid stocks are more likely to be manipulated and manipulation increases stock volatility. Imisiker and Tas (2011) presented from Istanbul stock exchange, small firms, firms with less free float rate and a higher leverage ratio are more prone to stock price manipulation.

Theory of corporate governance and financial crisis

In 2008, OECD also stated that the financial crisis revealed severe shortcomings in corporate governance.

Winter (2011) pointed that after the governance crisis 2001-2003 and the regulatory response through the Sarbanes Oxley Act and the European CG codes, the financial crisis has revealed persistent governance problems in financial institutions relating to executives, non executives and shareholders. Also, Ezzine and Olivero (2013) found out that effective governance mechanisms enhance the ability of firms to absorb a stock market crisis. Guota et al (2013) pointed that there is the lack of significant impact of corporate governance quality on performance. And well governed firms do not outperform poorly governed firms.

Hence, we can see, there exist various views on corporate governance and its importance.

Research methodology

Firstly, we analyze and compare corporate governance principles in each groups including: 1) Group 1 – Limited Western European CG representative standards including Belgian Code 2009 and The Netherlands Corporate Governance Principles;

Secondly, We also use, but not limited to, international standards of corporate governance such as: ICGN and OECD Corporate Governance Principles and Enhancing Banking CG Code 1999 which have many modifications in corporate governance principles after the crisis period.

Then, we propose what so-called limited comparative Western European corporate governance principles which are aiming to create a basic background for relevant corporations interesting in different aspects of corporate governance subjects and functions as the recommendation to relevant countries' government and other relevant organizations for public policy and necessary evaluation.

Last but not least, for a summary of our standards, see Exhibit and the below table 1 and 2 in relevant sessions.

Empirical findings

A- Findings on Corporate governance issues after financial crisis, corporate scandals and market manipulation

Some certain popular issues including: the roles and duties of CEO and senior management.

Also, we can find out another corporate governance (CG) issue. It is, the lack of descriptions of an effective risk management system.

B- Findings on Ways of Manipulation during Corporate Scandals

Several Manipulation Techniques found out during corporate scandals involve, but not limited to:

B.1 – The manipulation techniques in the income statement:

In Waste Management Scandal (1998), a Houston publicly traded waste management firm, there is a report of \$1.7 b in fake income.

B.2 - The manipulation techniques in both the income statement and balance sheet:

In the case of Refco financial service company, based in New York, entered the crisis and Chapter 11 in 2005 when its CEO had concealed \$430 b in bad debts.

B.3 - The manipulation techniques relevant to international accounting practice code:

In the scandal case of Global Crossing Ltd., a telecommunication firm, there is a failure in using international accounting standards (GAAP) in making financial reports. The company did not fairly present financial statements.

B.4 - Other manipulation techniques net belong to above classifications:

In some scandals, there is management manipulation which causes the loss of investments. In the case of Worldcom, a telecomm scandal, directors have used false accounting methods to manipulate stock prices after falling.

C- Actions on Preventing or Controlling negative manipulation

Among necessary actions to control negative market manipulation are, but not limited to, the mechanism of the board and its committees aiming to increase effectiveness and transparency with investors. Accounting and financial reporting process are also taken into account.

D- Findings on Construction of Comparative Western European Corporate Governance Standards

These findings will be shown in a detailed analysis of a model indicated in the later sessions.

<D.1> - Limited Western European Corporate Governance standards analysis

The Belgium Code of Corporate Governance 2009

The Belgian Code 2009 has been modified from its first version in 2004.

Among its advantages are, but not limited to, CG charter and CG statement. CG statement of the annual report covers a description of operation of committees, whereas CG charter includes direct or indirect relationship of the firm and major shareholders.

Generally speaking, The Code focuses on Board, Committees and disclosure of remuneration policy of executive managers mentioned in the CG statement. (see Exhibit 1).

The Netherlands Corporate Governance Principles

The Netherlands Best practices 2006 cover some major CG matters such as board roles and risk management.

Different from other European Codes, one of its distinctions is clarifying roles of supervisory board (SB). For example, SB should meet regularly and retain effective control over the firm.

For more information, please see Exhibit 2. However, it would be better to mention guidelines of CEO roles.

Comparison between the Belgian and the Netherlands Corporate Governance Principles

A lot of information on roles of Board is in the Belgian Code 2009. For example, it pointed Board ensures the integrity and timely disclosure of the firm F.S. But it would be better to give guidelines for a compliance officer. (see Exhibit 1).

On the other hand, the Netherlands Code stated roles of SB in ensuring appropriate plans and policies for the firm. Besides, it also oversees business performance.

Table 1 – A so-called Limited Western European CG representative standards

| Subjects or parties | Main quality factors | Sub quality factors |
|----------------------------|---|---|
| Audit committee | AC discuss significant financial reporting issues with EA and executive MGT; meet at least 4 times a year; twice a year meet IA and EA to discuss weakness of IC; | New AC members provided with IC, RM, operational, financial, accounting and auditing information; |
| CEO and The Chair | Consider positive and negative aspects if board considered the former CEO as chairman; | Chairman consults with CEO setting board meeting agenda; |
| Corporate Secretary | Ensure good information flow within board, committee, executive MGT and NEDs; | Advise board on all governance matters; regularly report to board; |
| Compliance officer | A compliance committee installed, or a high level compliance | Can be company lawyer; |

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| Board of Directors | officer appointed; No individual or group dominate board's decision making; organizing meetings using internet, video or telephone; | Ensure accuracy and completeness of CG charter and CG statement; |
| Independent director | Independency of judgement and objectivity in making board decisions; | Not an executive member of board; |
| Supervisory board to the Management | SB ensures individuals involved in daily MGT are of professional, integrity and social and moral; | SB ensures MGT take follow-up actions on supervisory recommendations; |
| Supervisory to the Board of Directors | Meet regularly and retain effective control over the firm | Committee of SB comprises a majority of unrelated supervisory directors; the engagement of an outside adviser; |
| Internal control | A framework of IC set by executive MGT approved by board; | Main risks identified and managed; |
| Internal audit | AC review IA work program; | AC recommends appointment/removal head of IA |
| External audit | Examine with AC safety measures taken to decrease risks; | Comment on the true and fair view of the firm assets and liabilities, financial positions; report AC key matters of FS; |
| Disclosure and transparency Shareholders | SB ensures timely and accurate disclosure; Controlling shareholders can appoint representatives to the board; Board ensures its obligations to shareholders are met; | Executive MGT prepare firm disclosure of F.S; Controlling shareholders can appoint representatives to the board; |
| The corporation as a whole entity | Has CG code with provisions and guidelines on how the firm implements the provisions of the code; | CG charter on firm website and CG statement on annual report; |

Conclusion

To overcome weaknesses from CG during crises, The Belgian Code 2009 suggested Board roles are important and skills, experience and knowledge of new board candidate should be evaluated (see Exhibit 1).

Besides, the Netherlands Code included guidelines for supervisory board (SB) including an orientation and education program for new members of SB.

In consideration of corporate governance issues analyzed in the previous sessions, we proposed the main and sub quality factors in this paper a **set of general comparative Western European corporate governance standards** in a limited model with selected countries. Though limited, it has some implications for further research and proper recommendations to relevant

government and organizations. And it also provides relevant academic and non-academic, lawyer and consultant, board and non-board people with minimum information for further researches.

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Exhibit

Exhibit 1 – The 2009 Belgian Code of Corporate Governance (a short summary evaluation)

| Subjects or parties | Main quality factors | Sub quality factors | Responsibilities | Objectives | Note |
|--------------------------------------|---|---|---|---|-------------|
| Audit committee | Chairman of the board should not be chair of AC; at least 1 with accounting and auditing expertise; | Review IA function; Set up by board; | Terms mentioned in CG charter; New AC members provided with IC, RM, operational, financial, accounting and auditing information; | <u>Not mentioned clearly in the code;</u> | |
| Nomination committee | Assist board on nomination and planning of CEO; majority comprises independent NEDs; | Set up by board; has remuneration report; with basic, variable remuneration, pension; | Terms mentioned in CG charter; recommend suitable candidates for board; recommends appointment CEO; meet at least twice a year; | <u>Not mentioned clearly in the code;</u> | |
| Compensation, Remuneration committee | Meet at least twice a year; | Set up by board; remuneration to attract, retain, motivate directors; | Terms mentioned in CG charter; make proposals to board; | <u>Not mentioned clearly in the code;</u> | |
| CEO /President/ MD | <u>Not mentioned clearly in the code;</u> | Join meetings of remuneration committee; | Clear division of duties b.t running the board and running firm business; | <u>Not mentioned clearly in the code;</u> | |
| The Chair | Promote effective interaction b.t executive MGT and board; | Take necessary measures to develop a climate of trust; | Should not be the same CEO; ensure directors receive accurate, clear and timely information; ensure all directors make knowledgeable contributions to board discussion; | <u>Not mentioned clearly in the code;</u> | |
| CEO and The Chair relationship | Chairman fully respect executive responsibilities of CEO; | Chairman supports, advises CEO; division of duties clarified; | Chairman establishes close relationship with CEO; | <u>Not mentioned clearly in the code;</u> | |
| Corporate Secretary | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | Board describes roles and tasks of secretary; | <u>Not mentioned clearly in the code;</u> | |
| Compliance officer | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | |

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| Board of Directors | <u>code;</u> Independent (at least 3 NEDs) | <u>code;</u> One tier board; pay attention to CSR, gender and diversity; | Terms mentioned in CG charter; adapts its governance structure to evolving needs; ensure financial and HR resource in place; | Ensure effective monitor and control; |
| Executive/Representative director | Independence of judgement and objectivity in making board decisions; | In board; | Provide all business and financial information to board; | <u>Not mentioned clearly in the code;</u> |
| Non-executive director | Independence of judgement and objectivity in making board decisions; | In board; ½ board comprises NED; | Help develop strategies and key policies proposed by executive MGT; meet at least once a year w/o CEO and other EDs; | <u>Not mentioned clearly in the code;</u> |
| Independent director | Independence of judgement and objectivity in making board decisions; | Not an executive member of board; | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> |
| CFO | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | AC decides when CFO, CEO attend meeting; | <u>Not mentioned clearly in the code;</u> |
| Management team (Senior Administration) | Board decides structure, powers, duties of MGT; | Careful MGT of potential risks; executive MGT include all EDs; | Board reviews executive MGT performance; | <u>Not mentioned clearly in the code;</u> |
| Supervisory for the board | <u>Not mentioned clearly in the code;</u> | Proper supervision of conformity; | Directors have access to independent professional advice; | <u>Not mentioned clearly in the code;</u> |
| Supervisory for the managers | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | Acts by board; | <u>Not mentioned clearly in the code;</u> |
| Internal control | <u>Not mentioned clearly in the code;</u> | A framework of IC set by executive MGT approved by board; | Main features written in CG statement; executive MGT set IC systems to assess, identify, manage risks; | <u>Not mentioned clearly in the code;</u> |
| Internal or statutory audit | <u>Not mentioned clearly in the code;</u> | Guaranteed free access to board; | Board supervises IA function; | <u>Not mentioned clearly in the code;</u> |
| External | <u>Not</u> | Guarantee | Comment on the | In accordance with |

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| audit | <u>mentioned clearly in the code;</u> | d free access to board; | true and fair view of the firm assets and liabilities, financial positions; report AC key matters of FS; | financial reporting framework in Belgium; |
| Disclosure and transparency | Executive MGT prepare firm disclosure of F.S; | Through CG charter and CG statement; | Allow effective external monitoring; | A high level of transparency; promote effective dialogue with (potential) shareholders; |
| Shareholders and Minority Stockholder | A website section describes their rights to join GM; | Respect rights of minority shareholders ; | Controlling shareholders can appoint representatives to the board; Board ensures its obligations to shareholders are met; | <u>Not mentioned clearly in the code;</u> |
| Accountability | <u>Not mentioned clearly in the code;</u> | Demands on business leaders; | Executive MGT accountable to board for the discharge of its duties; | <u>Not mentioned clearly in the code;</u> |
| Leadership | <u>Not mentioned clearly in the code;</u> | Chairman responsible for leadership of board; | Board provides entrepreneur leadership; | <u>Not mentioned clearly in the code;</u> |
| Employee | <u>Not mentioned clearly in the code;</u> | AC decides whether senior employee join meeting; | At GM, directors answer questions which do not prejudice firm, employee, shareholders; | <u>Not mentioned clearly in the code;</u> |
| 3 rd parties and conflicts of interests | <u>Not mentioned clearly in the code;</u> | Have a policy; | Each board member avoid direct and indirect conflicts of interest; | <u>Not mentioned clearly in the code;</u> |
| Code of ethics (conduct) | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> |
| Group and subsidiaries | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | A policy for transactions with related firms included in CG charter; | <u>Not mentioned clearly in the code;</u> |
| CG Code itself | Set a proper balance b.t leadership, entrepreneurship and performance; as well as control and conformity; | Ensure leadership, integrity and transparency in the decision making process; | Help determines firm goals; one-tier board model; has principles, provisions and guidelines; | Create more and faster transparency; long term value creation; |
| Management system | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | Main features of risk MGT system mentioned in CG statement; | <u>Not mentioned clearly in the code;</u> |
| Note | The underlined part is describing some more works needed to be done for relevant subjects and parties. | | | |

Exhibit 2 – The Netherlands Code of Governance (a short summary evaluation)

| Subjects or parties | Main quality factors | Sub quality factors | Responsibilities | Objectives | Note |
|--------------------------------------|--|---|---|---|-------------|
| Audit committee | Maintain professional relationship with IA and EA; | Direct communication channels to IA and EA; | SB establish AC; | <u>Not mentioned clearly in the code;</u> | |
| Nomination committee | <u>Not mentioned clearly in the code;</u> | S.D selected through a formal process; | Has a nomination committee of supervisory directors (S.D); | <u>Not mentioned clearly in the code;</u> | |
| Compensation, Remuneration committee | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | |
| CEO /President/ MD | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | |
| The Chair | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | |
| CEO and The Chair relationship | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | |
| Corporate Secretary | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | |
| Compliance officer | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | A compliance committee installed, or a high level compliance officer appointed; | <u>Not mentioned clearly in the code;</u> | |
| Board of Directors | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | Adopt strategy; training senior MGT; | <u>Not mentioned clearly in the code;</u> | |
| Executive/Representative director | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | SB reviews compensation of ED, reflecting duties and risks; | <u>Not mentioned clearly in the code;</u> | |
| Non-executive director | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | |
| Independent director | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | |

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| CFO | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> |
| Management team (Senior Administration) | Meeting for objectives developed by SB; | Invited once a year to discuss mgt report; | Supervisory board develops position for senior mgt and limits to mgt duties; | SB ensure competent MGT on an ongoing basis; |
| Supervisory for the board | Approve/develop corporate objectives; | Function independently of mgt; appropriate structure and procedures; | Set adequate information, documentation and reporting system; | Monitor the operations and firm performance; |
| Supervisory for the managers | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | SB ensures individuals involved in daily MGT are of professional, integrity and social and moral; | <u>Not mentioned clearly in the code;</u> |
| Internal control | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | Supervisory board responsible for the integrity of IC and MIS; | <u>Not mentioned clearly in the code;</u> |
| Internal or statutory audit | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> |
| External audit | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> |
| Disclosure and transparency | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> |
| Shareholders and Minority Stockholder | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> |
| Accountability | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> |
| Leadership | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> |
| Employee | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> |
| 3 rd parties and conflicts of interests | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | Unrelated supervisory director free from any of interest; | <u>Not mentioned clearly in the code;</u> |
| Code of ethics | <u>Not mentioned</u> | <u>Not mentioned</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> |

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|------------------------|--|---|---|---|
| (conduct) | <u>clearly in the code;</u> | <u>clearly in the code;</u> | | |
| Group and subsidiaries | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> |
| CG Code itself | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | SB assign committee of S.D duties for developing firm approach to CG; | <u>Not mentioned clearly in the code;</u> |
| Management system | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> | <u>Not mentioned clearly in the code;</u> |
| Note | The underlined part is describing some more works needed to be done for relevant subjects and parties. | | | |