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## Background

The audit committee and other board members occupy center stage today in the wake of corporate governance reforms. Their challenges are numerous, with perhaps their biggest challenge that of satisfying increased regulatory compliance requirements while maintaining their overall effectiveness.

The Audit Committee Institute (ACI) platform offers directors and audit committee members the opportunity to gain the additional knowledge, enhanced competencies and personalized assistance they need to fulfill their demanding oversight roles.

The ACI, sponsored by KPMG, has been communicating with board and audit committee members on an international level since its formation in 1999. In Belgium, the ACI is in direct and regular contact with over 2.500 directors. Fundamentally, ACI programs support members by providing a focus on evolving issues, the sharing of best practices, and the opportunity to meet with their peers.

- The ACI publication *Shaping the Belgium Audit Committee Agenda* is the *Vademecum* for all Audit Committee members, providing them with the knowledge, tools and techniques to help them better fulfill their demanding mission.
- The *ACI Web site* ([www.audit-committee-institute.be](http://www.audit-committee-institute.be)) and the *Audit Committee Quarterly* periodical offer articles from the ACI on regulatory and technical matters, feature audit committee "hot topics," and include other content from our extensive resources.
- ACI *Roundtable Sessions* and *Seminars* provide an opportunity to gain first-hand experience, and for an exchange with peers and Audit Committee Institute professionals.

Audit committee members and other board members are looking for *focused knowledge* and the *sharing of best practices*. Registration at the ACI Web site provides them with this helpful range of tools *free of charge*.

Please refer to the ACI Web site for registration.  
([www.audit-committee-institute.be](http://www.audit-committee-institute.be))

# Welcome...

... to the latest edition of *Audit Committee Quarterly*, a publication designed to help keep audit committee members abreast of developments in corporate governance and related matters. For those of you new to the Audit Committee Institute (ACI), and this publication in particular, a brief outline of the background to the ACI is set out opposite.

**Enron's audit committee** was chaired by Robert Jaedicke, a distinguished accountant and former Dean of the Stanford Business School. The audit committee did not meet very frequently, only three or four times a year, with each meeting lasting less than two hours - not quite enough time to consider all the important issues on the agenda. Now, everyone can conclude on the audit committee's performance, as its minutes are freely available on the internet (findlaw.com).

Earlier, in the week of our latest ACI Roundtable, the CFO of Enron was sentenced to six years in prison, and other Enron executives will likely face many years behind bars. Our latest ACI Roundtable was therefore specifically organized in response to the perceived concerns of our members regarding their **personal liability as an audit committee member**: the relating Roundtable topics have been elaborated upon in an article on page 6.

Since many audit committees during this year-end period will be confronted with an **annual self-evaluation**, which, according to the *Code Lippens*, is crucial to audit committee effectiveness, an article on this important process has been included on page 10 of this newsletter.

Another typical year-end issue of importance to you is the **One-to-One Rule calculation and the assessment of the external auditor independence**. The relating Belgian Company Code articles in this respect have recently been modified. A practical summary of these modifications starts on page 14.

Looking forward to after the year-end, we would first remind you of the changes to the European Transparency Directive discussed in a previous *ACI Quarterly*, and secondly that your **yearly financial information may now be published on your Web site** without further obligation to publish these results in the Belgian newspapers. This is provided, of course, upon meet certain conditions as set out on page 22. Looking forward even further **European corporate governance developments** are discussed from page 11, including the **obligation to disclose an annual corporate governance statement as a specific section of the annual report**.

We continue our Audit Committee Resources series on page 25 where we bring you articles of interest from around the globe.

Many other fascinating topics are included in this newsletter and I personally recommend that you read it inside out. You may want to consider contributing to our **Global ACI Survey 2007** by completing the enclosed form. The results and concerns, will be published on our Web site and in our ACI newsletters such that you can then share them with your board.

I trust you will continue to enjoy the ongoing benefits of the ACI. Please contact us at [info@auditcommitteeinstitute.be](mailto:info@auditcommitteeinstitute.be) with any comments or suggestions of topics you would like to see included, and do visit our Website at [www.audit-committee-institute.be](http://www.audit-committee-institute.be) for further ACI information.



Theo Erauw  
Chairman ACI Belgium

# Finding a practical approach to executive remuneration

Executive remuneration has become an increasingly sensitive issue for the boards of listed companies. Public concern over the size of executive pay packets is a perennial issue, often receiving much attention during the reporting and AGM season, or when a CEO is let go or resigns and walks away with what some may regard as an excessive payout. The ability of shareholders to cast a vote at an AGM on their company's remuneration report continues to concern many boards — any adverse vote by shareholders certainly sends a strong message to both the board and the executive concerned.

Designing an effective executive remuneration strategy is a difficult and complex undertaking. It involves compromises. The exercise of judgment. It is unquestionably one of the more demanding tasks a board faces, and is an emerging area for enhanced governance and transparency.

To address these concerns, there are several key issues that boards—and their remuneration committees—should work through in developing and refining their remuneration policies and practices.

## Market forces

Most boards will say that when it comes to executive remuneration, they are responding to “market forces”. To understand those market forces, chances are the board will seek the advice of an external remuneration consultant. A recent survey by the U.S. Business Roundtable found that 85 percent of respondent companies had retained a compensation consultant during the past year.

One important development is that consultants are increasingly being engaged directly by boards, or by remuneration committees installed by the board following provision 5.4 of the *Code Lippens*, rather than the executive team. This is a positive

development; consultants should be in no doubt regarding who they work for.

Consultants will usually provide comprehensive benchmarking data on current remuneration levels by size of entity, industry and job description, producing a range of remuneration amounts considered appropriate to attract, retain and motivate the “right person” (following provision 7.1 of the *Code Lippens*).

Boards and remuneration committees need to appreciate that benchmarking is not as precise and certain as they may often wish. It is the remuneration consultant's role to assist the board and remuneration committee to understand the composition, structures and values of the differing remuneration packages in the context of the prevailing tax arrangements, which can, in turn, influence the structure of packages in different countries.

The purpose of the benchmarking is to help the remuneration committee structure a package that keeps pace with the market, but does not outpace it. The board's and investors' concern with remuneration levels being continually geared up can be addressed by better understanding of the structures and values of the packages. It is not a

matter of avoiding benchmarking, but of appreciating its limitations.

## Performance considerations

Clever boards certainly recognize that the composition and structure of a remuneration package is just as important as its euro value. The same Business Roundtable survey noted earlier revealed that 57 percent of surveyed companies had increased the performance element of their senior executive remuneration over the past year. Twenty percent of companies said they primarily adopted long-term goals in designing pay-for-performance measures, while 73 percent used a mix of long and short-term goals alone. Indeed, in many companies, the variable, performance-related elements of remuneration are increasing as a proportion of the total reward. This is not surprising, given that investors want to see more of the executives' compensation being at risk.

Deciding how business performance should be reflected in executive remuneration is difficult. There is no simple, one-size-fits-all solution. Markets can fail to recognize strong management performance in the face of adverse circumstances because immediate outcomes turn out worse



than expected. Yet surely, one of the key tests of management is its ability to perform under adverse circumstances, including those not of its own making. After all, it is vital that management avoids turning a setback into a disaster.

In the context of executive remuneration, it is important that business success be clearly defined for both the executive and investors. The company's short and long-term objectives will have been approved by the board. These objectives then need to be translated into relevant performance hurdles against which the executives' short and long-term rewards will be paid out. Simply aligning remuneration to some aspect of total shareholder return (TSR) may not be appropriate.

One of the issues often cited either for or against executive reward is that business outcomes can be influenced by factors over which executives have little or no control. The booming market, for example, may be artificially lifting the company's share price. In this case, a relative TSR may be the best hurdle by which to measure the company's performance. However, boards and remuneration committees are increasingly turning to performance measures other than a relative TSR. These may include the company's performance over the longer term (at least three years) in areas such as return on capital, investment in research and development, market penetration, safety, and others. Boards and remuneration committees that fully appreciate the somewhat complex accounting implications of market-based hurdles (such as TSR), coupled with the need to more closely align rewards with the company's

objectives, are considering hurdles other than the traditional TSR and earnings per share.

One of the current issues facing boards and remuneration committees is reconciling corporate time frames with individual expectations. While there may be investor pressure to make long-term performance periods up to five years, the average tenure of company CEOs is shorter than that. The vesting of long-term incentives should be based on the company's goals, and not the CEO's horizon.

### Ongoing governance

Boards are increasingly treating executive remuneration more rigorously, recognizing it as an important and ongoing governance issue. In particular, boards need to be mindful of the subtle pressures that can undermine the objectivity and independence of their consideration of executive remuneration. A recent U.S. book has provoked debate over exactly this issue. Bebchuk and Fried argue that managers exercise too much influence over directors when it comes to remuneration matters. This influence tends to be informal and subtle, and owes much to the ability of U.S. CEOs and senior executives to influence board appointments. The Belgian situation is, of course, somewhat different. Nevertheless, the onus is on independent, non-executive directors to take an arm's-length approach to executive remuneration, establishing a dedicated board remuneration committee, and engaging their own independent remuneration consultants.

### Questions the board should ask:

- Is there a need for a formal board remuneration committee (*Code Lippens* Principle 5 Provision 5.4)?
- Does the remuneration committee have the requisite skills to understand the increasing complexity of executive remuneration? (Composition of remuneration committee: refer to *Code Lippens* Appendix E)
- Are the remuneration procedures compliant with the *Code Lippens* provisions as stipulated in relation to the *Code Lippens* Principle 7 of "reasonable remuneration"?
- Is the remuneration philosophy and strategy clearly articulated?
- How do remuneration issues fit into our organization, its culture and its strategy?
- Does the remuneration philosophy reflect careful consideration of the competitive landscape?
- Is the executive remuneration properly aligned with the business strategy?
- Is remuneration competitive with market levels?
- How is variable remuneration linked to particular levels of performance?
- Is the remuneration consultant independent and objective?
- Does the remuneration consultant report directly—and only—to the board remuneration committee?
- What are the accounting and tax implications?

# Personal data is not just a legal issue

The use of personal data is big business. Companies are able to capture more data about their customers than ever before, and are able to use this to refine and expand their offerings. As one would expect, this area of business is heavily regulated, namely under European Data Protection legislation, which also applies for many organisations outside the European Economic Area. Businesses appear to be keenly aware of its requirements, however there is growing evidence that there are other issues attached to the use of personal data which are not receiving all the attention they deserve.

The term “privacy” is commonly used to describe a set of rights that individuals are legally afforded, and as a set of obligations to which organizations and governments are legally required to adhere. The term is used throughout this article to refer to the way organizations manage the use of personal data.

Many organizations devise legally-orientated compliance programs. Generally, these programs are consistently strong at ensuring legal regulatory compliance, but are much weaker when they drill down into the control processes which are necessary to establish operational compliance and prevent compliance breaches. It is essential for organizations to ensure that their privacy policy is mapped into their business processes and IT systems to ensure that the organization is both legally and operationally compliant, and has appropriate mechanisms in place to deliver its privacy obligations.

Once developed and implemented, a system of internal controls that delivers operational compliance for privacy should be monitored by the compliance function and tested by internal audit. However, evidence suggests that, due to a lack of privacy auditing standards and methodology, privacy auditing is frequently not executed. Or, where it is, there remains the possibility of “false positives” from audit findings, and a latent amount of unforeseen risk.

There is evidence to suggest that privacy has become central to the notion of “trust”. The implication is profound. Being trusted allows an organization to capture greater and more accurate data, and this in turn can affect financial performance through improved customer retention, acquisition and increased spend.

- 86 percent of U.S./EU consumers have become more distrustful of corporations within the past five years (Datamonitor 2005).
- 68 percent of 32,000 respondents considered privacy to be related to a trusted corporate reputation (Ponemon Institute 2005).





- 84 percent of 250 senior risk managers agreed that risks affecting organizational reputation have increased significantly over past five years, and ranked reputation risk as the biggest threat to their organizations (Economist Intelligence Unit 2006).
- 64 percent of 32,000 consumers consented to secondary data use in high-privacy-trust Fortune 500 companies, compared to 51 percent in low-privacy-trust companies (Ponemon Institute 2005).

### The Audit Committee's role

The board of directors is required, at least annually, to conduct a review of the effectiveness of the group's system of internal controls, including financial, operational and compliance controls and risk management systems. The review should extend to include how the organization manages and controls privacy risk.

This review may well fall under the remit of the audit committee unless there is a separate risk committee. The committee charged with carrying out this review should consider the following issues when speaking to management:

- **Privacy controllability:** To what degree can privacy risk be identified and control achieved?
- **Privacy auditability:** How efficiently are controls executed, monitored and tested?
- **Privacy sustainability:** How are the controls maintained? To what extent are the controls resistant to system and process changes?
- **Privacy transparency:** To what degree can a true compliance level be determined at any given point in time?

### Conclusion

It is becoming more important for organizations to recognise the business value of managing personal data as a business asset, and to establish proper systems to protect and manage it. As governance failures continue to be reported around the world, it is also crucial to demonstrate to customers and employees that an organization can manage their personal data in a trustworthy and responsible manner.

# Roundtable on liability of Audit Committee members

28 September 2006



Enron's audit committee was chaired by Robert Jaedicke, a distinguished accountant and former Dean of the Stanford Business School. The audit committee did not meet very frequently, only three or four times a year, with each meeting lasting less than two hours—not quite enough time to consider all the important issues on the agenda. Now, everyone can conclude on the audit committee's performance, as its minutes are freely available on the internet ([findlaw.com](http://findlaw.com)).

Earlier, in the week of our ACI Roundtable, the CFO of Enron was sentenced to six years in prison, and other Enron executives will likely face many years behind bars. The founder of Enron told his jury: "I guess you could say [that] in the last few years, I have been living the American nightmare."

Audit committee members in Belgium are catching up to America by having nightmares as well these days. Indeed, from our previous Roundtable session and from our International Survey on Audit Committee practices, we learned that they are quite concerned about their potential liability as audit committee members. This ACI Roundtable was organized in response to those concerns, and, based on the display of intense interest, denial of responsibility does not offer much comfort to many.

Mr. Koen Geens, partner and lawyer at the Eubelius legal practice and associate

professor at KU Leuven, refreshed participants' memories relating to the general and specific liabilities of board members, including the *clear gross negligence concept* stipulated in Article 530 of the Belgian Company Code. Referring to the *clear professional error concept* contained in Article 527, Mr. Geens revealed to us a hidden dual paradox: first in the marginal judgment of general liability, and secondly, the judgment of the individual board member, versus the liability in solidarity with the Board. Concluding his introduction, Mr. Geens offered some practical knowledge pertaining to the complete and appropriate granting of discharge, which can never be binding toward minority shareholders, or in the case of incomplete information or fraud.

Ms. Hilde Laga, partner and lawyer at the Laga legal practice and professor at KU Leuven, Mr. Koen Geens, and Mr. Baron Valère Croes, President of the Audit Committee of Electrabel and Tessenderlo Chemie and member of the Audit Committee of Immobel, vividly and knowledgeably responded to the questions raised by our panel chairman Theo Erauw.

When an audit committee is asked to use its atypical "One-to-One" rule power of decision, as stipulated in Article 133 of the Belgian Company Code (as opposed to a merely advisory role for the audit committee established in Article 522—please refer to the ACI Quarterly 03 issue for an elaboration

## Those absent are always in the wrong...

of this matter), the advice of our panel members was to first formally inquire with the requesting party, e.g., the CFO, to secondly formally evaluate the request within the audit committee, and to finally have the decision of the audit committee formally adopted by the Board of Directors. "The judgment on the 'One-to-One' rule exception indeed relates to the independence of the external auditor," Hilde Laga commented, "as such a decision reaches out to the true and fair view of the financial statements, which is a responsibility of the board as a whole"

According to the Belgian Corporate Governance Code (*Code Lippens* - § 5.1), the terms of reference of the audit committee, including its role and the authority delegated to it by the board, should be disclosed in a corporate governance charter, and made available to the public via the company's Web site. Limiting the liability of the audit committee by limiting these terms of reference is not a viable option according to our panel members.

Firstly, the audit committee serves the responsibility of the board of directors, which cannot possibly be limited by any terms of reference. Secondly, the terms of reference, as well as the corporate governance chapter in the annual report of the board of directors, must be transparent and very clear in explaining any deviations from the *Code Lippens*. Although for the moment this corporate governance



code is not law, and therefore imposes no obligation as such, it is likely to serve as a primary best practice reference for courts when judging in corporate governance-related cases, as illustrated by ample references to the Dutch *Commission Peters Code* in the *Hollandse Beton Groep (HBG)* case.

Completeness and transparency should also be the norm in the reporting and minutes of the audit committee without, however, including unnecessary details or personal statements. Referring to the advisory role of the audit committee, its meetings should be held some days before the board of directors, and its meeting minutes should be attached to the agenda and other information addressed to the board.

A last but interesting question raised by our Roundtable participants was whether one could limit his or her personal liabilities by not being present at audit committee or board meetings. Our panel members concluded that this would be too easy, and on the contrary, increased one's liability. They referred to the general liabilities of board members who, in the case of claims resulting from errors, should not only demonstrate that they have not committed or been part of these errors, but who should equally demonstrate that they have not been capable of preventing these errors — a clear case that those absent are always in the wrong...

# U.S. Developments

## Fair Value Measurements

Statement 157, *Fair-Value Measurements*, establishes a single authoritative definition of fair-value, sets out a framework for measuring fair-value, and requires additional disclosures about fair-value measurements. The Statement applies only to fair-value measurements that are already required or permitted by other accounting standards, and is expected to increase the consistency of those measurements. The Statement imposes no requirements for additional fair-value measures in financial statements.

## Employers' Accounting for Defined Benefit Pension and Post-retirement Plans

Statement 158, *Employers' Accounting for Defined Benefit Pension and Postretirement Plans*, requires employers to recognize on their balance sheets the funded status of pension and other post-retirement benefit plans as of 31 December 2006 for calendar-year public companies. Employers will recognize actuarial gains and losses, prior service cost, and any remaining transition amounts from the initial application of Statements 87 and 106 when recognizing a plan's funded status, with the offset to accumulated, other comprehensive income. This could cause many employers that sponsor benefit plans to report significantly increased liabilities with corresponding reductions in equity.

In addition, the new Statement will require fiscal year-end measurement of plan assets and benefit obligations, eliminating the use of earlier measurement dates currently permissible. The new measurement date requirement will not be effective until fiscal years ending after 15 December 2008.

## Accounting for income tax uncertainties

The FASB recently issued Interpretation 48 in an attempt to increase relevance and comparability in financial reporting of income taxes. The Interpretation will directly affect the calculation of income taxes payable, and may also affect the measurement of deferred taxes. The Interpretation requires significant new annual disclosures in the notes to the financial statements.

The Interpretation mandates a two-step process in accounting for uncertainty in income taxes. The first step is to determine whether a tax benefit should be recognized. If the threshold is met, the second step is to determine the measurement of the benefit. Earlier authoritative literature provided no specific guidance. Some companies historically recognized tax positions only if they were "probable" of being ultimately realized, guided by views expressed by the SEC staff. However, research by the FASB staff suggested there was diversity in practice



with respect to the recognition and measurement principles used, and the scope of transactions to which such principles were applied. The new interpretation should result in more consistent application.

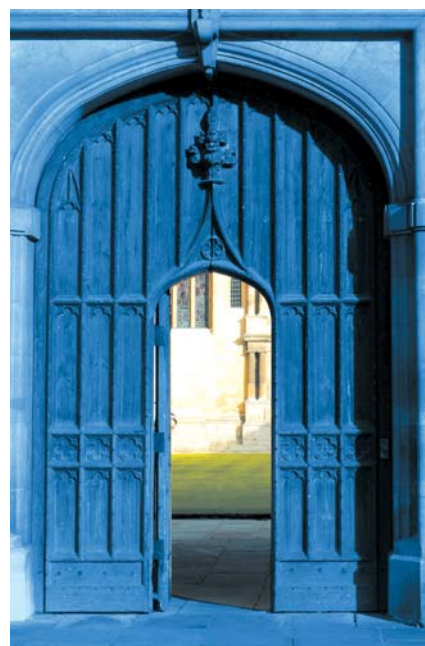
The Interpretation defines the confidence level (threshold) that a tax position must meet in order to be recognized in the financial statements as “more-likely-than-not” (more than 50 percent). In making this assessment, a company must assume that the taxing authority will examine the position and have full knowledge of all relevant information. Each tax position needs to be considered individually, and must continue to meet the more-likely-than-not threshold each reporting period. If a tax position is not considered more-likely-than-not of being sustained, no benefits of the position are to be recognized.

A company's position that a benefit meets the more-likely-than-not threshold may be supported, in whole or in part, by unambiguous tax law, an unqualified tax opinion from a qualified expert, prior experience with the taxing authority, an analysis prepared by management that considers all relevant facts, circumstances, and regulations, including widely understood administrative practices and precedents of the taxing authority.

The benefit recognition of a tax position meeting the more-likely-than-not criterion is measured based on the largest benefit that is more than 50 percent likely to be realized. The measurement is determined by considering the probabilities of the amounts that could be realized upon ultimate settlement with the taxing authority, assuming the taxing authority has full knowledge of all relevant facts. New information about a tax position should trigger a re-evaluation.

Interest that the tax law requires to be paid on the underpayment of taxes should be accrued on the difference between the amount claimed and the tax benefit recognized in the financial statements.

The interpretation is effective as of the beginning of the first fiscal year beginning after 15 December 2006. At adoption, companies must adjust their financial statements to reflect only those tax positions that are more-likely-than-not to be sustained as of the adoption date. The necessary adjustment should be recorded to the beginning balance of retained earnings in the period of adoption. The interpretation also requires significant new disclosures, among which is a table disclosing the beginning and ending balances of unrecognized tax benefits.



# Audit Committee Self-evaluation

The Audit Committee Institute recently published the results of its International Survey, taken from among its members. Comparing the Belgian results of the survey to the rest of the world reveals some significant findings:

- Members of Belgian audit committees are generally less satisfied with the effectiveness of their audit committee practices.
- One out of three members is dissatisfied with their current audit committee self-evaluation, compared to only one in ten internationally.

Transposing the primary results of this international survey to the current Belgian situation, many audit committees during this year-end period will unavoidably be confronted with an annual self-evaluation, which, according to the *Code Lippens*, is crucial to audit committee effectiveness.

## Setting the Belgium “scene”

In Belgium, the corporate governance *Code Lippens*, applicable to Belgian listed companies, adopted as of 2005 the following compliance principle: the audit committee should annually review its terms of reference and its effectiveness, and recommend to the board any necessary changes. In addition, according to best practices, the board should also make their own assessment of the performance of their audit committee's effectiveness.

## A three-step approach to an effective audit committee self-evaluation

Audit committees can organize several steps regarding their self-assessment:

### Step 1: First discuss the evaluation process to be adopted

Audit committees should determine which approach they want to use, i.e.:

- Who will coordinate the evaluation process?
- Who will set up a self-assessment questionnaire?
- Who will be in charge of compiling the results?
- Will the self-assessment be undertaken as a facilitated group activity?
- Who will participate in providing initial and additional input? (The CEO, CFO, head of Internal Audit, the external auditor, or others who interact with the audit committee)

### Step 2: The self-assessment questionnaire or facilitated group assessment

Once a self-assessment questionnaire has been prepared, each audit committee member and other dedicated parties opted will complete it independently. Once the results are consolidated, the audit committee can have an open discussion, led by its chairman, that i.e., focuses on the areas which clearly need improvement or where there is a great variation in answers. The compiled report must reflect each response and the mean rating, possibly also reflecting the overall average (the mean of the audit committee members and other participants), as the basis of a discussion regarding the committee's effectiveness and areas for improvement.

For a suggested framework of such a self-assessment, please refer to the Audit Committee Institute's publication available on the ACI Web site *Shaping the Audit Agenda - Toolkit*, as set out in Exhibit 4.



Alternatively, the self-assessment could be undertaken as a facilitated group activity led by the chairman of the audit committee or even an external party.

### Step 3: Results weighting aspects and reporting

During the evaluation session, the audit committee may wish to give more weight to some aspects than others. According to best practices, appropriate weighting will be influenced by a number of factors, among which are:

- The audit committee's charter and terms of reference
- The company's strategies, risk assessments and internal control environment
- The outcome of previous self-assessments
- The stage of maturity of the audit committee
- The views of stakeholders on the company's corporate governance performance
- Current and emerging business and economic factors.

The results of the self-assessment and any action plans or recommendations should then be reported to the board of directors.

# EU Corporate Governance developments

The European strategy regarding modernizing of company law and accounting rules has become, in part, a fact. This means that the concept of corporate governance and the ascendancy of the audit committee are, for the near future, a basic characteristic of European companies whose securities are admitted to trading on a regulated market, and which have their registered office in the EU member states.

Fundamentally, these initiatives consist of modernizing the Eighth Company Law Directive and the accounting directives; strengthening the regulatory framework in the European Union; reinforcing at Community level public oversight of the audit profession; imposing the use of International Standards on Auditing (ISAs) for statutory audits in the European Union; improving the systems of disciplinary sanctions, and establishing the transparency of audit firms and networks of such firms. In regard to *corporate governance*, initiatives include *reinforcing audit committees* and internal controls; strengthening auditor independence and introducing a code of ethics; facilitating the establishment of audit firms, and examining auditor liability.

## 1. The modernized Eight Directive and the audit committee

On 21 May 2003 the Commission adopted a communication on reinforcing the statutory audit in the European Union. Noting the progress made with regard to financial information, statutory audit, corporate governance and securities markets, the Commission, via this communication, pressed ahead its vision of a modern regulatory framework for statutory audits in the European Union.

The modernizing of the Eighth Directive became effective from the adoption of Directive 2006/43/EC by the European Parliament and by the Council on 17 May 2006 for statutory audits of annual accounts and consolidated accounts. The act amended Council Directives 78/660/EEC (Fourth Directive) and 83/349/EEC (Seventh Directive), and repealed Council Directive 84/253/EEC (Eighth Directive). It has been published in the Official Journal of 9 June 2006, with the deadline for adoption by the member states being **29 June 2008**.

The provisions regarding the audit committee are included in Articles 41 and 42 of the directive. The general principle reflected in these articles is that “*each public-interest entity shall have an audit committee*”. Moreover, the audit committee has a central role to assure the independence of the statutory auditor. We can extract two main contributions of the Eighth Directive as revised:

### 1.1 The audit committee helps to minimize financial, operational and compliance risks.

The articles observe that *audit committees and effective internal control systems* help to minimize financial, operational and compliance risks, and enhance the quality of financial reporting.

Member states might have regard to the Commission Recommendation of 15 February 2005 on the role of non-executive or supervisory directors of listed companies, and on the committees of the (supervisory) board, which sets out how audit committees should be established and function.



Member States may determine that the functions assigned to the audit committee or a body performing equivalent functions may be performed by the administrative or supervisory body as a whole.

With regard to the duties of the audit committee, the statutory auditor or audit firm should in no way be subordinated to the committee.

#### 1.2 The audit committee contributes to assure auditor independence.

To reinforce the independence of auditors of public-interest entities, the key audit partner(s) auditing such entities should rotate. To organize such rotation, member states should require a change of key audit partners dealing with an audited entity, while allowing the audit firm with which the key audit partners are associated to continue being the statutory auditor of such entity (internal rotation).

The auditor must communicate and declare his independence to the audit committee on a regular basis.

## 2. The Fourth and Seventh Directives modified

Another step forward has been accomplished since the adoption of Directive 2006/46/EC by the European Parliament and the Council on 14 June 2006. The global approach of this directive is to establish the collective responsibility of board members. Among other things, this directive introduced some transparency rules and, also for Companies whose securities are admitted to trading on a regulated market and which have their registered office in the Community, the obligation "to disclose an annual corporate governance statement as a specific and clearly identifiable section of the annual report." Member states shall bring into force the laws, regulations and administrative provisions necessary to comply with this directive by **5 September 2008** at the latest.

### 2.1 Changes brought by Directive 2006/46

To enhance confidence in the financial statements and annual reports published by European companies, the directive modifies the Fourth and Seventh accounting directives with four main new provisions.

**1. Establish the collective responsibility of board members:** Confidence in the financial statements is linked to those who have responsibility for their preparation and publishing. In line with what is currently prevailing in member states, the responsibility should rest collectively with all board members.

**2. Enhance transparency of related party transactions:** Company transactions with its managers, management's family members, or other so-called related parties are often not carried out under normal commercial conditions. While satisfactory transparency is required for all listed European companies, more transparency is necessary for unlisted companies under International Accounting Standards (IAS).



**3. Enhance transparency of off-balance sheet arrangements:** The disclosure requirements in the Accounting Directives for off-balance sheet commitments should be strengthened. Special Purpose Entities (SPE) serve as prominent example. They are captured in the balance sheet if they qualify as a subsidiary, but in many cases SPEs may be organized in a different way. Instead of developing complex definitions of an SPE (bearing the immediate risk of circumvention), disclosure should instead be improved by imposing a specific requirement in the notes to the accounts for material off-balance sheet arrangements, including SPEs.

**4. Introduce a corporate governance statement:** Investors on European capital markets have a major interest in listed EU companies' corporate governance practices. Accordingly, each listed company should — in a specific section of its annual report — disclose information about its practices in a “corporate governance statement”.

In this analysis, we focus on the corporate governance statement with regard to the particular evolution it contains.

## 2.2 Corporate governance statement and the Code Lippens

The Belgian Code on corporate governance (*Code Lippens*) which was published 9 December 2004 reflects the option of the flexible approach based on a “comply or explain” system. This approach is also favored by the OECD and is now reflected in the directive.

The justification of this position is founded on the observation that the strict and rigid application of a detailed set of rules would not allow the taking into account of companies' specifics, such as size, shareholding structure, activities, exposure to risks, and management structure. A code based on a rigid approach would therefore be unlikely to be followed by the companies at which it is aimed.

It is important to note that, by its incorporation in the EU Directive, the obligation of a corporate governance statement will now enter into law, as opposed to the “soft law” best practices of the *Code Lippens*. The United Kingdom, Germany, The Netherlands and the U.S. already have provisions in their legislation regarding such a “corporate governance statement” in the annual report for listed companies.

## Conclusion

In line with the Action Plan for modernizing company law and corporate governance, and with a view to further enhancing confidence in the financial statements and annual reports published by European companies, the European authorities intend to enhance the role of the audit committee in the Eighth Directive. Member states must provide a central role for the audit committee by 29 June 2008 at the latest.

The audit committee should be one of the key elements in the independence of auditors of public-interest entities in Europe in the near future.

Furthermore, by 5 September 2008 at the latest, a corporate governance statement will be included in the annual report for European listed companies.

# Changes to the Audit Committee assessment of EA independence

The Belgian law of 20 July 2006 introduced changes to the provisions of the Company Code with regard to auditor independence and the One-to-One Rule (Articles 133 and 134 of the Company Code). The new rules come into effect for the financial years ending 7 August 2006 or later. The substantial changes to the provisions that are of importance for members of Belgian company audit committees are the following:

- 1) The competency to grant exceptions to the One-to-One fee limitation
- 2) The calculation of the basis for the application of the One-to-One Rule
- 3) The scope for performance of incompatible services
- 4) Disclosure requirements.

## I. Competency to grant exceptions to the One-to-One Rule<sup>1</sup> (Modified Article 133 §6 of the Company Code)

The modified Paragraph 6 of Article 133 is intended to clarify the possible granting of exceptions to the one-to-one limitation for the provision of non-audit services. From now on, such exception can not only be granted by the audit committee of the Belgian audited company, but **also by the parent company's audit committee**, whether Belgian or foreign.

However, not all audit committees of foreign parent companies can now grant the abovementioned exception. Only if the foreign company is organized in accordance with the laws of a member state of the European Union or of an OECD member state (which are considered jurisdictions offering sufficient guarantees with regard to *corporate governance*) shall the audit committee of that parent company be able to grant an exception for a Belgian subsidiary.

Since different bodies share the same competency to grant exceptions to the One-to-One Rule, being an audit committee or the ACCOM<sup>2</sup>, the legislature has stipulated that when a derogation is decided upon by an audit committee, it should not be possible to seek approval from ACCOM, and *vice versa*.

Finally, the decision granting the exception and its motivation must be **disclosed in the financial statements**, an obligation meant to increase transparency in this matter.

<sup>1</sup>The "One-to-One Rule" applies to listed companies and companies that are part of a group that is required to publish consolidated annual accounts.

<sup>2</sup>The Advisory and Control Committee on the Independence of the External Auditor, as established by the Royal Decree of 4 April 2003

## II. Calculation of the basis for application of the One-to-One Rule (Modified Article 133 §7 of the Company Code)

With its modification of Paragraph 7 of Article 133, the legislature intends to clarify the calculation needed to apply the One-to-One Rule.

Following the amendment, the calculation should now be performed **on a global basis** for the audited company and its subsidiaries, and no longer per stand-alone entity. As such, the one-to-one comparison should now be calculated per financial year as follows:

Total fees for COMPATIBLE NON-AUDIT SERVICES performed by the statutory auditor or its global network to the benefit of the audited company or its subsidiaries (Belgian or foreign)

----- compared to -----

Total fees for STATUTORY AUDIT MANDATES performed by the statutory auditor or its global network to the benefit of the audited company or its subsidiaries (Belgian or foreign<sup>1</sup>)

## III. The scope for performance of incompatible services (Modified Article 133 §8 of the Company Code)

The modified provision defines, with more precision, the scope within which non-audit services, incompatible with auditor independence, are forbidden.

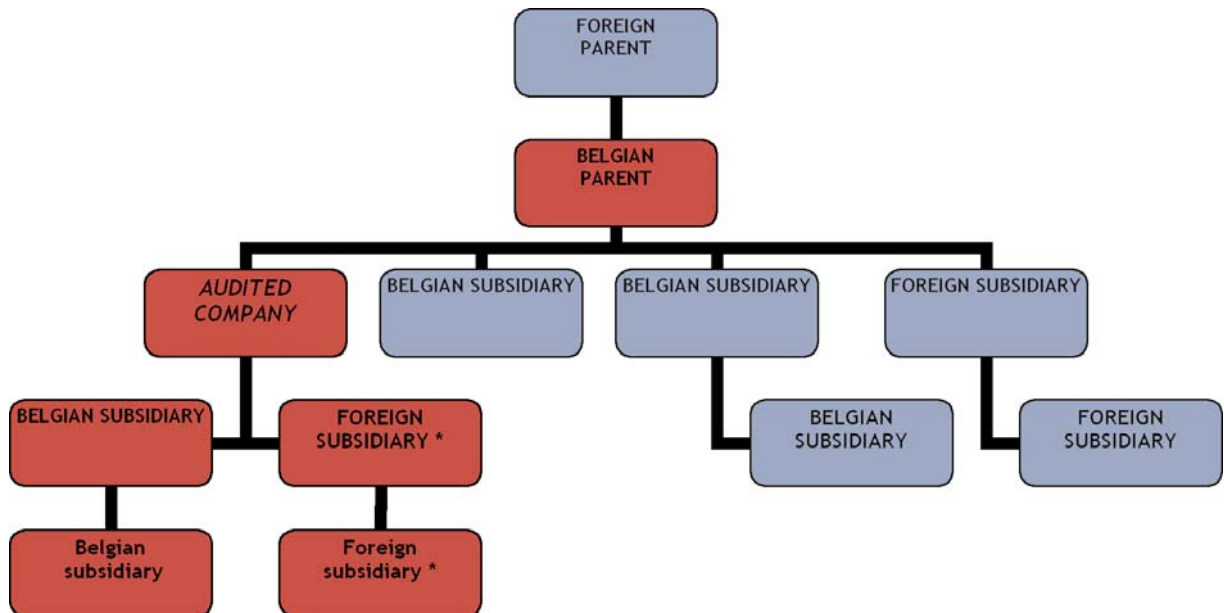
<sup>1</sup>For foreign subsidiaries, the fees must be calculated in accordance with the provisions of domestic law applicable to each specific subsidiary.

Under the modified provision, it will not be possible under Belgian law to perform the defined incompatible non-audit services without compromising the auditor's independence in the following scenarios:

| Provided by   | To whom   | Which services   |
|---|---|--|
| The statutory auditor or its <b>global</b> network  | <ul style="list-style-type: none"> <li>- Belgian audited company</li> <li>- Belgian companies controlling the audited company</li> <li>- Belgian subsidiaries of the audited company</li> </ul> | Articles 22 and 24: Member States shall ensure that statutory auditors or audit firms that carry out the statutory audit of a public interest entity |
| The statutory auditor or its <b>Belgian</b> network | - Foreign subsidiaries of the audited company   | Incompatible services listed in Art. 183ter of the Royal Decree of 30 January 2001   |

The new provision makes it now clear that it is indeed possible for the statutory auditor or its Belgian network to provide incompatible non-audit services to Belgian or foreign collateral companies (so-called "sister" companies).

The above could be summarized as follows:



\* Incompatible services are prohibited based on Article 183ter of RD of 30 January 2001 for services rendered by the auditor and its Belgian network. Foreign law provision for services rendered by the foreign network of the auditor

#### IV. Modified Disclosure Requirements (Modified Article 134 of the Company Code)

The modified Article 134 of the Company Code now requires the disclosure of the amounts of *the statutory audit fees* (for companies listed in Belgium, and companies that are obliged to prepare and file consolidated financial statements in Belgium) and the amount and nature of *non-audit fees* (for all companies) in the annex to the annual accounts (or consolidated annual accounts). Previously, only non-audit fees were required to be disclosed in the annual report of the board of directors. This provision was modified in order to facilitate the verification of the adherence to the One-to-One Rule.

The legislature has now provided also for a disclosure in three categories, which are the following:

- Other verification assignments (e.g., reports relating to contributions in kind, mergers and de-mergers, valuations of options on shares that are not listed on a stock market, alteration of legal form, liquidation, Fost +, Val-I-Pac etc.)
- Tax advice assignments
- Other non-audit assignments (e.g., non-tax due diligence, advice on environmental matters, etc.).

#### V. Conclusion

From the preparatory documents, the legislature's intention has clearly been the clarification of certain aspects regarding the independence of the statutory auditor, including the rendering of non-audit services by the statutory auditor and his network. Further modifications of the above rules are to be expected, however, as new questions may be brought. The members of audit committees in Belgium must take into account the changes to the provisions which are in effect for the financial years ending on **7 August 2006** or later. Please refer to the full text of the Belgian law of 20 July 2006, which appeared in the Belgian Official Gazette of **28 July 2006**.



# Global ACI Survey on Audit Committee effectiveness



Audit committee members around the globe are moderately positive about their committee's effectiveness, about the quality of the oversight process, the committee's self-evaluation and its relationships with executives and auditors. But, on every one of these topics, they feel there is certainly room for improvement.

Most of the rules, legislation and guidance for companies that has been produced over the last ten years have the same underlying objective: to improve the way organizations are controlled and, in turn, creating greater shareholder value. Much of this guidance has focused on the role of the audit committee and the execution of its duties. It would thus seem appropriate to ask audit committee members how effective they felt their audit committees were.

That's why Audit Committee Institutes (ACIs) around the world posed a series of 30-plus questions to audit committee members of public and non-public companies. The survey was held through early 2006. These queries, ranging from very broad questions (*How effective is the audit committee?*) to more focused questions (*How much time did you spend fulfilling your audit committee role in 2005?*) were all aimed at identifying the key challenges and concerns driving audit committee activities world-wide.

## Effectiveness

In the central question of audit committee effectiveness, the results of the survey show a gap between the United States and Europe. While 72 percent of U.S. audit committee members rate their audit committees as "very effective," these scores are much lower in the UK (52 percent), Canada (64 percent), Australia (57 percent), The Netherlands (48 percent), Belgium (30 percent) and France (22 percent).

One reason for the trans-atlantic difference in these results may be that in the European principle-based environment, it is more difficult to rate and benchmark effectiveness. In the American rule-based environment, one can seek full compliance which can be rated as "very effective". Also, it is possible that U.S. audit committee members consider themselves most effective because audit committees were established in the U.S. earlier, thereby allowing them to "perfect the art"; so to speak. Of course, these results indicate "perceived" effectiveness, and U.S. audit committee members may believe that going through the Sarbanes-Oxley process in itself helps ensure audit committee effectiveness.

Cultural differences may also be a reason for the variation between the European and U.S. results. Perhaps Europeans are more reserved when asked to self-evaluate performance, or perhaps they feel that there is always room for improvement.

## *“Somewhat satisfactory, with room for improvement”*

### Room for improvement

Although these effectiveness ratings should be viewed as positive, many audit committee members feel there is room for improvement. Indeed, taking the “needs improvement” and “somewhat effective” ratings as one, a substantial global proportion feels that their audit committees could improve on their performance: the UK (48 percent), The Netherlands (52 percent), the U.S. (28 percent), Canada (36 percent) and Australia (44 percent). Interestingly, the combined score is 78 percent in France, presenting a stark contrast to the global trend. In France, 23 percent felt their audit committee needed improvement and only 22 percent rated it “very effective”.

Despite complaints of regulation overload, three out of four audit committee members feel their effectiveness has improved over the past year.

### Oversight processes

For an audit committee to become effective, it should have pre-audit committee meeting materials of sufficient quality. Sixty percent of the respondents say their pre-meeting materials are of “high quality”. Interestingly, while the French rate their audit committee effectiveness lowest of all countries surveyed, they rate the quality of their pre-audit committee meeting materials the highest (80 percent). We may conclude from this that the quality of information they receive is not an obstacle to their effectiveness.

Even when the pre-meeting materials are satisfactory, the effectiveness of the audit committee will, to a significant extent, depend on the time it has available to execute its duties. Although French respondents rated their meeting materials of the highest quality, they were the least satisfied with the amount of time they had to dedicate to their role as audit committee members. Indeed, 67 percent stated they needed more time, or at best, were only somewhat satisfied with the time available. This compares to Belgium (71 percent), the UK (42 percent), The Netherlands (48 percent), the U.S. (31 percent), Canada (40 percent) and Australia (38 percent).

Another factor contributing to effectiveness is a well constructed agenda and work plan. Nearly all respondents say they are at least “somewhat satisfied” with the approach used to establish the audit committee work plan, although four out of ten say there is room for improvement.

### Self evaluation

Performance evaluation is a relatively new concept in audit committees—and indeed in supervisory boards—and where procedures are in place, the approaches vary. Globally, audit committee members are fairly satisfied that their self-evaluation process enhances the committee’s effectiveness. On the other hand, 70 percent feel that the committee’s current self-evaluation approach could be improved.

In Europe, the picture is very mixed. The majority of respondents were only somewhat satisfied that performance evaluation enhanced audit committee effectiveness. The proportion of respondents dissatisfied with the process was highest in Belgium (36 percent) and France (17 percent), and lowest in the UK (3 percent) and The Netherlands (4 percent). Most respondents rated the board as communicating the most constructive feedback to the audit committee. The UK, Belgium, The Netherlands, the U.S. and Canada all rated the external auditor positively in this regard.

### Relationships and communications

Audit committee members generally were most satisfied with their interaction with, and the support they receive from the CFO. This was followed by the chief audit executive (internal audit), the external audit partner, and the CEO, respectively. In all regions, respondents were least satisfied with their interaction with, and support from the company's external legal counsel.

Nearly three in every four respondents said their audit committee is very effective at ensuring the external auditor's independence from management and its accountability to the audit committee. Respondents in the Americas were the most confident in this respect, followed by Australia, Europe, and South Africa, respectively. Nearly half of the respondents in Asia were only "somewhat satisfied" in their audit committee's ability to ensure the external auditor's independence and accountability.

### Fear of litigation

Fear of litigation is not just an issue in the United States, and concerns over exposure to personal financial loss as an audit committee member are widespread. However the UK, Belgium and The Netherlands are much less concerned about financial exposure than their U.S. counterparts. Still, some 75 percent express moderate concern while 25 percent of the Belgian audit committee members are "very concerned," compared with 26 percent in the United States. Audit committee members feel particularly exposed given the nature of their responsibilities. While many countries have unitary boards and every director is equally responsible in theory, the very nature of the audit committee role tends to give rise to greater exposure. Whether or not this is a real or perceived threat, our respondents feel they are more exposed than their fellow board members. Interestingly, despite their concern about financial exposure, 99 percent of the respondents are at least "somewhat satisfied" with their personal liability insurance coverage, and even 36 percent seem to feel completely safe, stating that they are "very satisfied" with their insurance policy.

### Summary

Audit committees around the world generally feel they are fairly effective at ensuring the integrity of the financial reporting process. Most are confident they are able to ensure the independence of the external auditor from management, and its accountability to the audit committee. Also, most are satisfied with the support they receive from the CFO, chief audit executive, external auditor, CEO, and full board.

However, nearly half of the audit committee members today consider the committee as being only "somewhat effective." Most audit committee members cite significant room for improvement in various aspects of the oversight process, including agenda-setting, self-evaluation, pre-meeting materials, and the chief audit executive's accountability to the audit committee.

The full version of the Survey can be downloaded from [www.audit-committee-institute.be](http://www.audit-committee-institute.be).

## General features and regional characteristics

| Audit Committee Characteristic | Audit committees around the world often...  | Significant Regional Differences   |
|--------------------------------|---|--|
| Composition and Background     | <ul style="list-style-type: none"> <li>• Have three or four members</li> <li>• Have backgrounds as a CFO (or related accounting/finance experience) and broad business experience</li> <li>• Feel it is "very important" for one or more members to have financial reporting/accounting expertise</li> <li>• Consider "contacts" and "public profile" as the least important prerequisites for serving as a member</li> </ul> | <ul style="list-style-type: none"> <li>• South Africa: largest average audit committee membership (five)</li> </ul>  |
| Time commitment                | <ul style="list-style-type: none"> <li>• Devote less than 100 hours to fulfilling their audit committee role</li> <li>• Serve on only one or two audit committees</li> </ul>  | <ul style="list-style-type: none"> <li>• Americas: more than 80 percent of audit committee members devoted 50 hours or more fulfilling their role</li> <li>• Asia: only 44 percent devoted more than 50 hours</li> <li>• Asia: members are most likely to serve on three or four audit committees</li> </ul> |
| Meetings/mechanics             | <ul style="list-style-type: none"> <li>• Met approximately seven times last year (five face-to-face meetings and two teleconference calls)</li> <li>• Conducted face-to-face meetings that averaged three hours and teleconference calls lasting half as long</li> </ul>  | <ul style="list-style-type: none"> <li>• Americas: averaged most meetings per year (eight)</li> <li>• Asia: Fewest meetings conducted via teleconference (virtually none)</li> </ul>   |
| Liability/exposure             | <ul style="list-style-type: none"> <li>• Feel that legal/financial exposure is greater for audit committee members than for other board members (and are duly concerned)</li> <li>• Are quite satisfied with their directors' and officers' liability insurance coverage</li> </ul>   | <ul style="list-style-type: none"> <li>• South Africa and Asia: four in ten say legal/financial exposure is "significantly greater"</li> </ul>   |

## Global ACI Survey 2007

Do you feel that your audit committee has become more effective over the past year—or less effective? Do your peers share your views and concerns?

To better understand the challenges and issues facing audit committees today, the Audit Committee Institute (ACI) has launched the Annual Audit Committee Survey 2007. We expect to generate valuable insights into current practices, emerging trends, and prospective issues affecting audit committees with this annual survey.

To ensure that your views and concerns are included, please take a few minutes to complete this survey. (It should take approximately 10 minutes, and may be completed on-line at our ACI web site [www.audit-committee-institute.be](http://www.audit-committee-institute.be). In return, the results will be published on our web site and in our ACI newsletters such that you can share them with your board. We kindly ask you to complete this survey by 15 January 2007.

Thank you in advance for your participation. We are confident that you will find this annual survey to be a vital resource for better understanding your audit committee's challenges—and shaping its future agenda.

# No more press releases in the Belgian newspapers

Listed companies in Belgium may publish their annual and interim financial results on their Web site as of 1 January 2007. A further obligation to publish these results in the Belgian newspapers has been abolished. It is expected most companies will elect to publish via the Web only.

## Publication via the Web site

Following the amendment of the Royal Decree of 31 March 2003 by the Royal Decree of 4 October 2006, listed companies in Belgium may publish all required annual and interim financial information via their Web site only, provided that this information is available no later than the moment of its public announcement.

Further, the Web site shall meet the following requirements:

- The financial and obligatory information shall be presented in a separate and updated section of the Web site and needs to be accessible to everyone free of charge.
- The Web site shall contain a “financial calendar” scheduling the periodic publications by the entity, and shall announce any publication delays.
- The Web site shall offer to shareholders and other interested parties the possibility to subscribe to a mailing list to be provided with the information free of charge at the moment of announcement.
- The Web site shall contain all information published during the preceding three years.
- The Web site shall equally display all warnings and information published by the Banking, Finance and Insurance Commission (BFIC) relating to the entity.

The BFIC has the right to enforce additional technical conditions.



### Publication via the Newspaper

The presentation of information via the Web site may, under certain conditions, be replaced by publishing in one or more national newspapers, or in a newspaper with a large readership throughout Belgium. Issuers subject to foreign law are allowed to keep the information accessible at locations mentioned in advertisements placed in one or more newspapers distributed nationally or in large editions throughout Belgium.

### Publication of inside information

As well, inside information (art. 6 §1 1° RD) does not have to be published on the Web if published in one or more newspapers distributed nationally or in large edition throughout Belgium or, if the information is presented on the Web site of the market operator organizing the market on which the financial instruments of the issuer are being traded.

### Publication of an advertisement

Finally, there are still other kinds of information for which an advertisement is sufficient. Such advertisements contain an indication of where the public information can be found. Subsequently, a publication on the entity's Web site is not required. This particularly concerns:

- The annual financial statements (statutory and consolidated), the annual report and the auditors report (Art. 10 RD). (Please note that from now on these documents should be presented in the format of a brochure.)
- The special reports mentioned in the Company Code and the proposal documents relating to changes of the articles of establishment or association (Art. 11 RD).

### BFIC and market operator

The listed company shall provide all information which is required to be made public to the BFIC and to the market operator without delay, and no later than at the moment of announcement to the public or the shareholders.



# European Union: Council approves Code of Conduct on Transfer Pricing documentation

Within the EU, almost every member state has its own transfer pricing regulations and country-specific transfer pricing documentation requirements. For multinationals, this diversity in requirements has led to a significant increase in compliance costs. In addition, multinationals are audited more frequently by the tax administrations within the EU on the correctness of their transfer prices.

To harmonize documentation requirements and reduce the related costs for multinationals within the EU, the European Commission set up the EU Joint Transfer Pricing Forum in 2002. Within this forum, both tax administrations and business representatives meet regularly to discuss transfer pricing issues. This discussion of transfer pricing documentation requirements by the Forum has resulted in a Code of Conduct being proposed by the European Commission, and its recent approval by the European Council of Ministers. Multinationals must carefully assess how they set and document their transfer prices within the EU.

## Council approves Code of Conduct

The Code of Conduct on Transfer Pricing Documentation is intended to harmonise documentation that multinationals must provide regarding their pricing of intra-group transactions (their "transfer prices") to the different tax administrations within the EU.

After the European Commission approved the proposal for the Code of Conduct on Transfer Pricing Documentation on 10 November 2005, based on the work of the EU Joint Transfer Pricing Forum, the Council of Ministers approved the Code of Conduct on Transfer Pricing Documentation 27 June 2006. It is now up to the member states to implement the Code of Conduct at a national level.

## EU TPD-concept is essential

The essential point in the Code of Conduct is the concept of EU Transfer Pricing Documentation (EU TPD). The EU TPD will constitute the transfer pricing documentation within the EU for multinational groups opting for the EU TPD concept, and consists of:

- The *Masterfile* (a set of documents containing a blueprint of the group and its transfer pricing policy, and which will be available to all involved member states), and
- *Country-specific documentation* (documentation per Member State containing information specific to the Member State in question).

For certain multinational groups, opting for the EU TPD can lead to a reduction of compliance costs.

## Opting for the EU TPD

Opting for the EU TPD concept must be carefully considered by each multinational group on a case-by-case basis. In balancing the advantages and disadvantages, one must take into account the specific characteristics of

the involved group members within the EU (especially exercised functions, assumed risks and invested means), the underlying facts (e.g., important modifications in the supply chain), and the current agreements with local tax administrations (e.g., concluded transfer pricing rulings).

## Implementation by the member states

It is now up to the member states to implement this Code of Conduct in their national regulations. This can occur through a change in the law, but also through the issue of a circular letter. A number of member states, including the Czech Republic, Denmark, Spain and Sweden, have already taken the content of the Code of Conduct into account while preparing and/or drafting new transfer pricing legislation. Other member states are likely to follow in due course.

## Transfer pricing issue should be taken up to board level

In order to be sure that its transfer pricing policy is acceptable for tax administrations, and is documented in an efficient way to meet the various documentation requirements within the EU while remaining a useful tool to optimize its shareholders value, a multinational group and its Board must pay sufficient time and resources to the transfer pricing issue.



# Resources

## New rules governing the liquidation of commercial companies

*The Belgian Federal Parliament amended the Company Code by adopting a new law this summer to improve the liquidation procedure (Wet tot wijziging van het Wetboek van vennootschappen, teneinde de vereffeningprocedure te verbeteren/ Loi modifiant le Code des sociétés en vue d'améliorer la procédure de liquidation).*

The new law was adopted mainly in the interest of the creditors of companies that are being liquidated. Its aim is to make the liquidation procedure more transparent and to avoid abuses.

The existing Article 184 of the Company Code is replaced by a new article providing that the commercial courts must validate the appointment of a liquidator decided by the general assembly of shareholders. In principle, the liquidator's functions start only as of the date its appointment is validated by the Court. Any acts committed by the liquidator between the date of its appointment by the general assembly and the date of validation by the Court must also be validated by the Court. In order to obtain such validation, an application must be filed with the competent commercial court, together with a statement of the assets and liabilities of the company. The public prosecutor, as well as any interested third party can also file such an application.

Persons that have been convicted for theft, fraud, misappropriation of funds or other similar offences may not be appointed as a liquidator. Certain other categories of persons require the explicit authorization of the commercial court.

The commercial court can appoint a liquidator itself if it refuses to validate the nomination of the liquidator appointed by the shareholders. The Court can also declare null and void certain acts committed by the liquidator appointed by the general assembly.

The new law also adds other provisions to the Company Code. For example, a file is to be kept at the registrar's office of the competent commercial court concerning each liquidation containing a series of documents listed in the law. The liquidators must file a detailed report of the state of the liquidation proceedings at the registrar's office of the commercial court in the sixth and twelfth month of the first year of liquidation, and subsequently once every following year. Liquidators failing to file such detailed report may incur substantial fines.

At the end of the liquidation procedure, the liquidators must submit a proposal for the distribution of the assets to the competent commercial court for approval and the commercial court may request the liquidators to provide all required information to verify the validity of the distribution proposal.

Liquidators having been appointed before the publication of the Law of 2 June 2006 must comply with its provisions after a period of one year as from the publication date (26 June 2006).

## Managing and Auditing IT Vulnerabilities

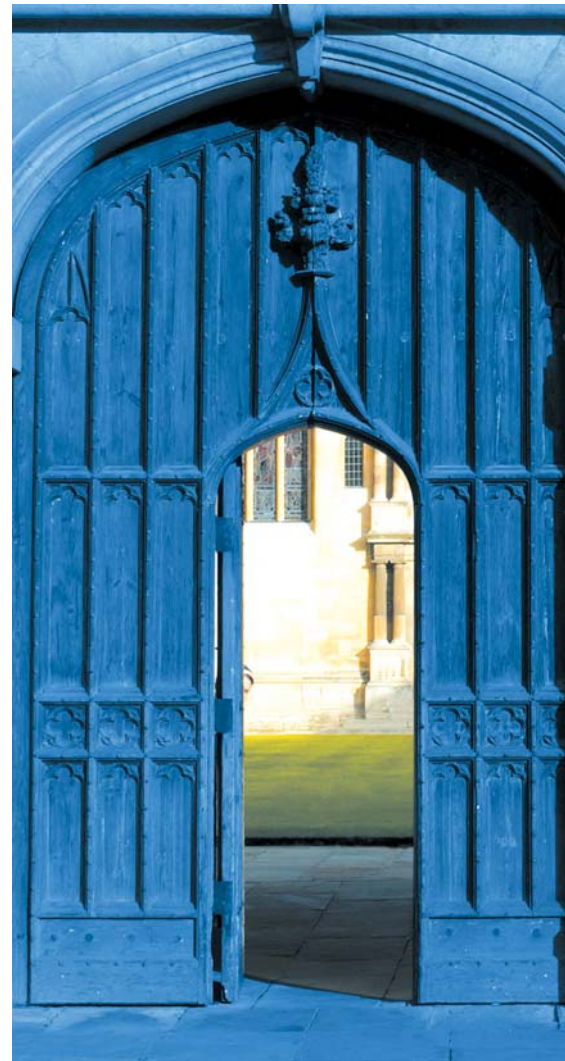
*The Institute of Internal Auditors (IIA) has recently released a sixth guide in its Global Technology Audit Guide (GTAG) series, Managing and Auditing IT Vulnerabilities. Vulnerability management is a set of processes that an organization employs to identify, assess, and mitigate business risks arising from the deployment and use of IT assets and processes.*

This GTAG issue was developed to help assess the effectiveness of an organization's vulnerability management processes by asking the right questions of IT security staff. It recommends practices to guide an organization toward achieving and sustaining higher levels of effectiveness and efficiency. After reading this 24-page guide, you will:

- Have a working knowledge of vulnerability management processes
- Have the ability to differentiate between high- and low-performing vulnerability management organizations
- Be familiar with the typical progression of capability: from a technology-based approach to a risk-based approach to an IT process-based approach
- Provide useful guidance to IT management on leading practices for vulnerability management.

The guide provides sample metrics to use when measuring vulnerability management practices, such as identifying the number of unique vulnerabilities, the percent of total systems that are subject to a configuration management process, and the mean time to remediate a problem. Finally, the guide lists the top 10 questions which should be asked about vulnerability management, and illustrates answers indicative of low- and high-performing organizations.

The Managing and Auditing IT Vulnerabilities guide may be downloaded free of charge from the Technology-GTAG section of the IIA Web site [www.theiia.org](http://www.theiia.org)



## Outside Director Liability Across Countries

*Settlements reached in 2005 in securities litigation involving Enron and WorldCom highlighted the financial risks faced by outside directors of public companies. The authors of this ECGI paper argue elsewhere that Enron and WorldCom, as instances where directors made damages payments out of their own pockets, are and likely will remain exceptional.*

The authors of this ECGI paper show that the risk of out-of-pocket payment is likewise very low on a cross-border basis outside the U.S., in both common law and civil law countries. The largest source of risk is efforts by government agencies to make an example of particular directors, even when the cost of doing so likely exceeds the financial recovery.

The authors study Britain and Germany in depth, and offer summaries of the position in Australia, Canada, France, and Japan. They find that while specific laws quite often differ, there is substantial functional convergence. In each country they analyze, due to a combination of substantive law, procedural rules, and market forces, the out-of-pocket liability risk faced by outside directors of public companies is similar-present but very small. Further, they draw upon cross-border analysis to assess the legal risks outside directors can expect to face going forward, both in the United States and elsewhere.

The Outside Director Liability Across Countries paper may be downloaded free of charge from the Publications - Working Paper Series section of the Web site of the European Corporate Governance Institute [www.ecgi.org](http://www.ecgi.org)



## Manager's Guide to Compliance: Sarbanes-Oxley, COSO, ERM, COBIT, IFRS, BASEL II, OMB's A-123, ASX 10, OECD Principles, Turnbull Guidance, Best Practices, and Case Studies

*Navigating the compliance landscape is never easy, and the lack of guidance in the marketplace makes simply understanding the relevant compliance requirements is often frustrating. By discussing a variety of hot topics under a single cover, Anthony Tarantino has attempted to assemble an introductory handbook for professionals in finance, information technology (IT) and operations. He has largely succeeded, delivering a book that's easy to read and navigate. Each of its 30 chapters is dedicated to a specific compliance topic, with an overview of the related compliance requirements.*

Tarantino provides an informative discussion on best practices in corporate governance and ethics—two essentials to compliance and risk management. Readers may also find useful his discussion on data-retention requirements and compliance project management. IT managers who are involved in designing or testing related IT controls should find the matrix that maps COBIT to COSO very informative, along with the related discussion on IT risk management and segregation of duties.

While the book does provide an outline of the different compliance requirements, readers should not expect a practical compliance handbook. However, given the book's general nature, anyone seeking to better understand the relevant compliance requirements should consider it a "must-read," but be advised that the book was not written specifically for audit committees, and does not provide guidance on how to comply efficiently.

The book *Manager's Guide to Compliance* by Anthony Tarantino may be ordered from [www.amazon.com](http://www.amazon.com) and other specialist booksellers.

## Corporate Governance Codes and their Implementation

*Rules relating to corporate governance can be found in stock exchange regulations, company articles of association and also, recently, in coordinated corporate governance codes. The latter should not, however, be considered the equivalent to law or contractual provisions. Notably, the enforcement of corporate governance codes is a very complex matter, and has lately been explored in a personal working paper by Eddy Wymeersch, Professor at the University of Ghent Law School.*

Compliance is ensured first and foremost by internal mechanisms: the Board of Directors and management must take responsibility for applying the code under the overall guidance of the shareholders, whereas the market will provide the environment in which developments will thrive.

Outside monitoring—the auditor, the supervisor, the regulated market, or a review panel—may also be envisaged. However, their remit is generally restricted to formal assessment; judicial enforcement is not generally favored.

As stated by the European Corporate Governance Forum, the role of shareholders and of the general meeting deserves to be strengthened. This will contribute to better management of the company and accountability of the Board. By establishing a stronger link between market-led enforcement and internal governance instruments, the overall governance system is likely to be strengthened. This may be more successful than imposing formal legal or administrative requirements.



## ACI Events

### Roundtable Series

The ACI facilitates interactive audit committee roundtables twice a year. Every Roundtable features one or more guest speakers, and provides for an exchange of views and insights on topics of interest to members of boards and audit committees for a limited number of professionals.

The ACI roundtable sessions can provide you with knowledge you will find helpful in your increasingly responsible oversight role through a focus on current topics, enhanced competence by the sharing of best practices, and personalized assistance by providing opportunities for interaction with your peers.

The next Roundtable event will be organized in the **Spring 2007**.

### Seminars

The ACI Seminar is an exclusive event organized by the Audit Committee Institute for selected Board members who share similar challenges to their oversight Roles. The *Code Lippens* states under its fourth corporate governance principle that *"Directors should update their skills and improve their knowledge"*.

The next ACI Seminar will be held on Thursday **14 December 2006**. Members of audit committees and boards of listed and other large companies will receive a personal invitation to participate. Tailored to their specific needs from their Board oversight roles, the next ACI Seminar will feature experts bringing to them a high-level and practical update of major developments in the field of IFRS, tax and legal matters.



## About us

The Belgian Audit Committee Institute (ACI) was established with the purpose of providing members of audit committees and other board members with the knowledge required to carry out their responsibilities. The ACI follows developments in the field of governance, audit issues, accounting, and financial reporting, both in Belgium and internationally.

The professionals of the ACI are:

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