Revised Corporate Governance Code published

On 8 December 2016, the corporate governance committee ("Committee") published the final version of a revision of the corporate governance code ("Code") which will apply to financial years starting on or after 1 January 2017. The Code is restructured around a number of themes as opposed to the current code of 2008 (the "2008 Code") which is based on a functional division of roles and responsibilities within a company. Focus areas of the Committee in the Code are long term value creation, the importance of culture and the strengthening of the internal audit function and audit committee.

The key changes made to the Code, compared to the 2008 Code, are listed in further detail below. We believe the following changes are likely to have the most impact on companies applying the Code:

- In addition to the one non-independent supervisory board member allowed for under the 2008 Code, the revised independency rules in the Code allow for each shareholder holding 10% or more of the shares in the company to have a further non-independent affiliated member on the supervisory board (provided that the total number of non-independent members is less than half of the total number of supervisory board members).
- The variable part of a management board member's remuneration needs to be linked to predetermined and measurable performance criteria which predominantly have a long term character.
- Supervisory board members may serve a maximum of two terms of four years after which a he or she can be re-appointed for up to two additional two-year periods.
- The increased focus on internal risk management and related procedures, including required 'in control' statements.
- Additional requirements to explain deviations from the Code.
- All independence criteria to be met by the chairman of the supervisory board.

A number of proposals included in the consultation versions of the Code as published on 11 February 2016 and on 3 August 2016 (please see our client briefings of February 2016 and August 2016, respectively) did not make it into the Code. Notable ones are the proposal allowing for a share-based compensation of the supervisory board members, the proposal to delete the provision that holders of depositary receipts at all times have the right to receive a proxy to vote in shareholder meetings, and the proposal to require the management board to confirm that the continuity of the company is safeguarded for a period of 12 months.

The Committee advises that the chapter in the board report on corporate governance structure and compliance with the Code be tabled as a separate agenda item for discussion for the general meeting in 2018.

The Dutch government is expected to give its opinion on the Code and the Parliament may devote a session to it, after which the Code will be published in the *Official Gazette.*

Key changes to the Code

1. Comply or explain

- For each deviation from a Code provision, the company describes:
  i. how the company deviates;
  ii. the reason for the deviation;

iii. if the deviation is temporary and will last for more than one financial year, when the company intends to comply again; and

iv. what alternative approach, if any, has been adopted for any deviation and how this complies with the underlying objective of the relevant provision, or an explanation of how the alternative approach contributes to proper corporate governance of the company.

2. Strategy, long term value creation; risk management; in control statement

- The management board develops a view and formulates and implements a strategy on long term value creation, including risk control.
- The management board timely involves the supervisory board when developing a view and realising a strategy on long term value creation and the supervisory board supervises the implementation of its strategy.
- The management board analyses the key risks that the company faces and determines the company's risk appetite and relevant checks and balances.
- The management board confirms in the 'in control' statement in the board report that:
  i. the board report provides sufficient insights in any shortcomings of the internal risk control and risk management systems, also in relation to non-financial aspects;
  ii. these systems provide reasonable certainty as to the correctness of the financial reporting;
  iii. the current situation justifies financial reporting on a going concern basis; and
  iv. the report sets out material risks and uncertainties relevant for the company's continuity for a period of 12 months after the date of the board report.
- The management board and supervisory board draw up internal regulations on the reporting of (suspected) irregularities within the company, and establish further rules on the procedures to be followed and on the supervision thereof by the supervisory board.
- The management board promptly informs the chairman of the supervisory board of any signals of (suspected) material irregularities. The external auditor reports any (suspected) irregularities he comes across in the course of his activities to the chairman of the audit committee.

3. Internal audit function; audit committee; external accountant

- The internal audit function is strengthened and includes a clearer division of tasks between the internal auditor, the audit committee and the management board.
- The internal auditor has direct access to the external accountant and audit committee.
- Audit committee meetings are attended by the management board member responsible for financial matters, the internal auditor and the external accountant.
- The audit committee provides advice to the supervisory board on the selection, nomination and dismissal of the external accountant and in reporting on its functioning.

4. Appointment and functioning of boards

- Supervisory board members may serve two terms of four years after which such member can be re-appointed for up to two additional two-year periods, the reasons for which must be explained in the report of the supervisory board.[1]
- A management board member or supervisory board member resigns in case of malfunctioning, irreconcilable conflicts of interest or in other circumstances where the supervisory board considers it necessary. In that case, the company issues a press statement, stating the reason for the resignation.
- If a company has an executive committee, the board report sets out its role and functioning and the reasons for having such a committee. This description also covers the way in which the contact between executive committee and supervisory board is structured. In addition, the management board ensures an adequate exchange of information with the executive committee taking into account the checks and balances of a two-tier system, and the supervisory board supervises the dynamics between the management board and the executive committee.

[1] The new appointment terms set out in the Code do not apply to supervisory board members (i) who on the date of the Code's entry into force were already supervisory board member for longer than eight years, *provided that* in total they were not appointed for longer than 12 years; (ii) who will be appointed at the general meeting in 2017 for a third period of four years.

- If the composition of the management board or the supervisory board in terms of male/female ratio deviates from the company's diversity objectives and/or from thresholds set in applicable law, the corporate governance statement provides information on the current situation and explains how and when the company expects to achieve this ratio.
- The management board assesses its functioning on an annual basis (as is currently already required for the supervisory board), both collectively and on an individual basis.
- Management board members and supervisory board members report to the supervisory board if and when they wish to accept a position with another company or entity. Prior approval from the supervisory board is required if a management board member wishes to become a supervisory board member of another company.
- The provisions on non-compete and corporate opportunities for management board members are extended to supervisory board members.
- Cross board memberships as such are no longer considered as a conflict of interest; the same applies to the mere appearance of a conflict of interest.
- The management board and the supervisory board should avoid conflicts of interest in case of a public bid, substantial acquisitions and disposals and other substantial changes in the company's structure. The management board ensures that the supervisory board is timely and closely involved. In case of a non-public bid on a substantial part of the company, the management board publishes its view and reasons as soon as possible.

5. Independent supervisory board members

- The Code maintains the existing independence criteria for supervisory board members as well as the restriction that at most one member may be non-independent. However, this restriction no longer applies in case of the following two of these independence criteria:
  - supervisory board members holding, directly or indirectly, more than 10% in the company's share capital; and
  - supervisory board members who are directors or representatives of legal entities holding, directly or indirectly, more than 10% in the company's share capital,

  provided, however, that:
  - the total number of non-independent supervisory board members is always less than half of the total number of supervisory board members; and
  - each person or entity holding more than 10% of the company's share capital (directly or indirectly) may only have one non-independent person appointed as supervisory board member.
- The supervisory board confirms compliance with the independence criteria in the report of the supervisory board.
- In addition to the independence criterion under the 2008 Code that he is not a former member of the management board, the chairman of the supervisory board meets all independence criteria as set out in the Code.
- The chairman of the supervisory board as well as a former management board member cannot act as chairman of the audit or remuneration committee.
- More than half of the members of each of the committees of the supervisory board should be independent within the meaning of the Code.

6. Remuneration

- The company has a clear and understandable remuneration policy that takes into account, amongst other things, the following aspects:
  - A proportionate variable component that is based on predetermined and measurable performance criteria that are predominantly long term oriented; and
  - The company's strategy on long term value creation.
- A management board member expresses its view on his or her own remuneration proposal, taking into account the different aspects of the company's remuneration policy.
- Shareholdings by supervisory board members in the company shall be long-term investment.
- The annual remuneration report, to be prepared by the remuneration committee, includes information on internal remuneration proportions and changes in such proportions in comparison to the previous year.

- Severance pay will not be awarded if the agreement is terminated early at the initiative of the management board member, or in the event of seriously culpable or negligent behaviour on the part of the management board member.

7. Response time

- If the management board invokes a response time in case shareholders propose an agenda item which may lead to a change in the company's strategy, it has to report on its actions at the end of this period and the supervisory board has to supervise this.

8. Culture

- The management board creates a culture of openness and integrity, aimed at long term value creation. The management board and the supervisory board are responsible for developing, safeguarding and embedding this culture.
- The management board determines common values that contribute to the creation of long term value; it develops a code of conduct and makes sure it is embraced by all employees; and provides an explanation in the board report on the way in which the culture in the company is given proper attention.

9. One-tier boards

- The chairman is independent in the meaning of the Code.
- The chairman of the board presides over the meetings of the board and he is responsible for a balanced composition of the board as a whole and of the board's committees and for their proper functioning.
- The chairman of the board or a former executive board member cannot be the chairman of the audit committee or the remuneration committee.
- The non-executive board members have to account for their supervision in the past financial year.

The consultation draft in relation to amendment of the provisions on one-tier boards as published on 3 August 2016 contained further guidance on how the Code should be applied to companies with a one-tier board, but this guidance was not incorporated in the Code.

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