

Monitoring Committee Corporate Governance Code
F.a.o. Mr. W.B. Kuijpers
P.O. Box 20201
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Rotterdam, July 9, 2008

CAV/AdB/iz/MCC019

Subject: Comment on the Committee's proposals for amendment of the Dutch Corporate Governance Code

Dear Mr Kuijpers,

We are pleased to respond to your invitation to comment on the Committee's proposals for amendment of the Dutch Corporate Governance Code ('the Code') as published on June 4 2008. We fully support your efforts for improved risk management and internal control practices and disclosures. Our comments focus on the Committee's proposed amendments of the Code's best practice provisions relating to external reporting on risk management and internal control.

According to an Ernst & Young survey, many investors admit that they are currently making decisions based on incomplete risk information. What they want is relevant information on significant, specific business risks. Almost 70% of investors prioritise transparency in their investment decisions. They value openness and communication above other factors when considering initial investments.ⁱ A recent survey commissioned by NIVRA and Eumedion concluded that only 62% of the Dutch listed companies provide information on the key risks related to their corporate strategy in their 2007 annual reports.ⁱⁱ

The empirical findings above support the Committee's position that there is substantial value in improved corporate disclosures around risk management and internal control. Investors' and other stakeholders' needs for improved risk information encompasses the entire portfolio of strategic, operational, (financial) reporting and compliance risks.

Both the internationally recognised COSO Enterprise Risk Management Framework as well as the respective (amended) European Council Directives, support the distinction made by the Committee between strategic and operational risks versus (financial) reporting and compliance risks. This distinction is rooted in the reality that the achievement of strategic and

ⁱ Ernst & Young global survey 'Investors on Risk - The Need for Transparency', November 2005.

ⁱⁱ 'Inzicht in onzekerheid. Onderzoek naar de risicoparagrafen in de jaarverslagen 2007 van beursfondsen', published by Shareholder Support, June 2008.

operational objectives -generally set by the entity itself- are typically not entirely within its control whilst the achievement of (financial) reporting and compliance objectives -generally based on standards imposed by external parties- are typically largely within an organisation's control.

In our view, the way in which the Committee tries to reflect the above in its proposed amendments to the Code's best practice provision II.1.4 ('in control statement') has two significant disadvantages:

- It directs management's attention primarily towards financial reporting risks while, as empirical studies have shown, more shareholder value has been destroyed as a result of strategic mismanagement and poor operational execution than in all of the (financial) reporting and compliance scandals combined;ⁱⁱⁱ
- The 'uniqueness' of the proposed amendments to The Netherlands poses challenges to the management of Dutch public multinational companies, as well as their investors, often operating under multiple jurisdictions and corporate governance regimes. The proposed new best practice provision II.1.4a is similar to for example the management attestation as required under Section 404 of the US Sarbanes-Oxley Act 2002, but has significant differences as to the time period covered by this attestation.

Close (r) alignment to an international recognised standard such as COSO would help mitigate these challenges.

Based on the above, we recommend the Committee adopt the following 'outline' for external reporting on (the adequacy and effectiveness of) risk management and internal control systems:

- An overview of the risks and uncertainties that are significant and specific to the company's objectives. This overview should consider strategic, operational, (financial) reporting as well compliance risks. In line with current Dutch company law, specific attention should be given to the company's market, credit, liquidity and cash-flow risks;
- An overview of the main objectives, components and attributes of its internal risk management and control systems relevant to the significant and specific risks identified, including -if applicable- the company's risk management objectives and policy for using financial instruments^{iv};
- An indication of the reference framework or system of standards management has used in reviewing its risk management and internal control systems;
- An overview of the process management applies for reviewing its risk management and internal control systems;
- An assessment of the adequacy and effectiveness of its risk management and internal control systems. Thereby indicating the extent to which management has reasonable assurance that:

ⁱⁱⁱ See for example 'Worrying About the Wrong Risks' by Paul Kocourek and Jim Newfrock in the March/May 2006 issue of The Corporate Board Magazine.

^{iv} In practice a company's strategic, operational, financial reporting and compliance control objectives and their related controls are often overlapping. This is true particularly for entity level controls but also for many controls at the application or transaction level. Therefore, when providing a high level description of these systems, it is often not possible to make meaningful distinctions between risk management and internal control systems aimed at reducing financial reporting risks and those aimed at mitigating strategic, operational and compliance risks.

- They understand to which extent the company's strategic and operational objectives are being met;
- The Company's internal and external (financial) reporting is reliable;
- Applicable laws and regulations are being complied with^v;
- An overview of important failings which have been discovered in the year under review or the current year, together with any changes made or improvements planned;
- Reference of the discussion(s) on the above with the Supervisory Board / Audit Committee.

We believe the external reporting outline above provides the following key advantages:


- It is faithful to the Code's principle-based approach and at the same time provides for a more meaningful and consistent application of its best practice provision II.1.4;
- It supports a more balanced and comprehensive approach towards the external reporting on the various types of risks and the manner in which they are controlled;
- It acknowledges the interdependencies between the various types of risks and the manner in which they are managed;
- It is fully aligned with an internationally recognized risk management framework (i.e. COSO);
- It stimulates companies to concentrate their disclosures and statements on risk management and internal control into one section of their annual report;
- It enhances comparability of risk (management) information, both between companies as well as for individual companies over time. This enhanced comparability will facilitate the assessment of the relevance and reliability of these disclosures and statements and thus their further improvements going forward.

To conclude, we hope you will find the above to be a relevant contribution to your efforts and would be happy to provide you with any additional information you may require.

Yours sincerely,
Ernst & Young Accountants LLP



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^v This definition of effectiveness is fully aligned with the one adopted by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in its September 2007 publication titled 'Enterprise Risk Management - Integrated Framework'. Page 24 of this publication states that: "When enterprise risk management is determined to be effective in each of the four categories of objectives, respectively, the board of directors and management have reasonable assurance that:

- ▶ They understand the extent to which the entity's strategic objectives are being achieved;
- ▶ They understand the extent to which the entity's operations objectives are being achieved;
- ▶ The entity's reporting is reliable;
- ▶ Applicable laws and regulations are being complied with.