

**Introduction to the 4th , 7th
& 8th EU Directives**

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This presentation provides a birds-eye view of the EU directives that form the platform for EuroSox implementation. Highlights are focussed on Governance, Risk and Compliance issues, Comply and Explain, Internal Controls and a preliminary to-do list.

International Regulatory Compliance Objectives

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External:

- Create trust in capital markets through supervision and regulation of those who seek to raise capital on these markets
- Allow investors to make an informed choice through the timely publication of reliable and relevant information and disclosures
- Ensure that corporate entities not only subscribe to but also comply with agreed norms for corporate governance

Internal:

- Protect shareholder interests and assets – through the establishment and function of a system of internal controls
- Ensure transparency & appropriate public reporting mechanisms
- Scandals have created overreactions in regulatory oversight.

- **The European Unions Financial Services Action Plan (FSAP)**
- The 4th directive Annual Accounts of specific types of companies
- The 7th directive Consolidated accounts
- **The 8th Company Law Directive on Statutory Audit**
 - Professional ethics, independence and objectivity
 - Auditing standards, Audit reporting, Auditors' liability
- **The 8th Company Law Directive and Corporate Governance**
 - The impact of mandates on Corporate Governance
 - Internal controls and external auditors
 - The European Group of Auditors' Oversight Bodies (EGAOB)
- **The Transparency Directive**
 - The 'harmonization' of Annual financial reports and disclosures
- **The Market Abuse Directive**
 - Insider dealing, Market manipulation, Lamfalussy process
- **The EU Data Protection Act**
 - At odds with SOX 806 (Anonymity of Whistleblowers)

- | | EU Articles |
|--|-------------|
| • 8th directive/SOX 404 | |
| • Revisionskomité / Audit Committee | 1 |
| • Effektivitet af interne kontrol- og Risikostyringssystemer /
Effectiveness of internal controls | 2b |
| • Intern kontrol vedrørende regnskabsaflæggelsen /
Internal control over financial reporting | 4 |
| • Væsentlige mangler / Material weaknesses | 4 |

Differences in perspective



- PCAOB
- COSO
- Rule based
- AS 2/5/IFRS
- Comply or die
- 404 Certification



- EGAOB
- Turnbull, COSO.
- Principal based
- IFRS/International Audit standards
- Comply or explain
- No Certification

Collective responsibility of board members for annual accounts

- Greater disclosure of **off-balance sheet arrangements** including intra-group relationships/transactions with unconsolidated subsidiaries (QSPE)
- Greater disclosure for **related party transactions**
- **Disclose risk management activities** in their annual reports and provide information on:
 - Principal elements of the **risk management system**
 - Key elements in implementing an **internal control system**, including how its effectiveness is monitored
 - **Corporate Governance code** which the company applies (Comply or Explain)

The Comply or Explain Principle

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- The “comply or explain” principle has become a feature of Europe’s approach to corporate governance.
- **Obligation to comply or explain.**
- **A high level of transparency**
- **Company boards ultimately accountable**
- Regulatory framework, as well as relevant and sufficient **shareholders rights.**
- The **corporate governance statement** is for
- **Review and discussion with the shareholders.**
- Regulatory authorities **reaction on misrepresentation of facts.**
- External auditors should review ‘element of facts’ in the statement.



Focus on the following

- Organization & Scoping - Areas your company should be in compliance
- Framework, Methodologies and Tools
- Facilitation, advice and assistance on Design and Implementation of Internal Controls
- Build a controllable “Governance, Risk and Compliance” mindset, positioned as a **set of services**
- **Holistic approach** to Governance, Risk and Compliance
- **Improved data quality** by focusing on policies and procedures at the transaction level
- Performance **insight at business unit levels** and react to changes

What are the general GRC Issues?

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Boards Slow To Move:

- Slow to take concrete and effective measures to realize international compliance.
- Management does not yet recognize importance of international compliance.

Top-Down approach:

- Laws only establish basic guidelines
- Take a wait and see approach.
- The-Top Down approach. Once a rule is implemented it will be followed?

Resistance to Change:

- Follow the crowd and resisting change
- View internal control as a tool management controls rather than a standard they have to conform to.

Transparency Issues:

- Management must overcome cultural obstacles of assessing their company's internal control components,

- **Establish audit committees**
 - Improving Corporate Governance.
 - Strike the balance between the benefits of additional requirements
 - Strike the balance between costs and burdens.
- The directives result in an **intensified disclosure from management.**
- Management is responsible to disclose a report that reflects a '**true picture**' of the situation in the company.
- A full **certification from the external auditors** is *still not* in the Governance, Risk and Compliance pipeline.

- Management's lack of **recognition of the importance of compliance.**
- **View internal controls as a tool rather than a international standard**
- Management must **assess the company's internal control components**
- Developing and implementing measures to achieve adequate internal control
- Other obstacles can be cultural, lack of uniformity in national legislation, resistance to change, Business as Usual, International Best Practices, Investor confidence.

- Focus the internal control audit on the **most important matters**
- Eliminate procedures that are unnecessary to achieve **intended benefits**
- Make the audit clearly **scalable** to fit any company's size and complexity
- Simplify the standard
 - **Dialogue** Between Auditors and Companies
“Critically Important”

Conclusions

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- Governance, Risk and Compliance is mainstream and requires focus
 - GRC goes beyond Internal Controls and Risk Assessment
- Set realistic goals. Managements commitment, Planning & Resources
- Top-down approach, including scope, Communication, Consistency, Segregation of duties, Culture, Specific Accounting issues
- Due to increased Regulatory Oversight ‘ in-house knowledge’ is essential Increased IT Applications implies more discipline
- Take a holistic approach. Focus on definable business benefits
- Give Internal Audit a strong role, but ownership belongs to line management

- **Organization of the compliance efforts**
- **Scoping - what areas of your company should be in compliance**
- **Framework, Methodologies and Tools**
- **Facilitation, advice and assistance on Design and Implementation of Internal Controls**
- **Test, Assessment and Audit**



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