





# Corporate Governance

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# Corporate Governance

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**Appendix**

**Appendix 1 – Additional detail about the best practices regarding  
Corporate Governance**



# 1. Introduction



## 1. Introduction

### Corporate Governance

*Corporate Governance* has been associated to the relation ***principal-agent problem***.



The investor (principal) hires a manager (agent) to administer the companies on their behalf.

*Corporate Governance* concerns how to ***align the interests of both parts*** and assure that the companies will be managed in the principal's benefits.

*Corporate Governance* is frequently associated with the **structure of management body of companies**.



## 1. Introduction

### O Corporate Governance – an increasing concern

The increasing concerns about organization's **sustainability**, **ethics** and **financial scandals** that recently occurred, have conducted to a closer look to which could be the best governance practice.

These concerns have been reflected:

- **Governments**, in the production of norms and regulations that seek to guide the implementation by organizations of best governance principles.
- **Organizational**: by implementing the corporate governance models.
- **Society in General**: with new institutes/ associations that focus on corporate governance.

In terms of **political power** is now a perfect awareness of the contribution that good corporate governance makes to **economic growth**, **investment** and **financial market stability**.



## 1. Introduction

### **Corporate Governance's objectives:**

The prime objectives to be achieved by corporate governance are:

- ensure integrity, professionalism and accountability of management;
- consider internal control mechanisms to encourage good management practices;
- predict appropriate mechanisms of transparency and reporting;
- establish supervision mechanisms that may contribute to the credibility of the global business environment.



## ❖ Decline in the Economy

As Economy walked into a recession at 2000, stock prices fallen.

The decreasing of stock prices was even deeper by the awareness of practices/behaviours non-ethics by some companies.

It is presented in the next slide some examples of fraud:



## ❖ Examples of committed fraud

### Enron

1. Used *special-purpose entities* (SPE) to decrease their responsibilities and to count **artificial income** for either SPE either Enron.
2. Contracts lasting for several years were accounted for in the first year, reducing costs and oversized income.

### WorldCom

1. **Current expenditure** were accounted as **investments** (with this they transformed the losses they indeed had in profits).
2. **Very large amount of loans** to top executives were not paid by them.

### Tyco

1. **Manipulated the accounts** to show high profits.
2. **Non-approved loans** to top executives (these executives used company's money to buy personal property and other assets).



## ❖ Studies regarding fraud

Other fraud examples were studied by **Agrawal, Jaffe, and Karpoff (1999)**.

They identified **103 companies** accused of **fraud** present at Wall Street Journal Index between 1981 and 1992. They have also established 103 control companies whose code of economic activity and net sales was similar to that of companies with fraud.

- The companies that were part of fraud's companies sample had significantly more fraud than the ones of the control group in the 2years before and 2years after regarding the year of the key event for the study.
- The differences in operating performance around the event of fraud were not statistically different between two groups.



Regarding rotation management they “**didn't find evidence that fraud revelation leads to a subsequent alteration in the leadership structure**” – in the cases which CEO and Chairman are the same person. They also evaluated the rotation for the tree top positions and the alterations remain non-significant between companies in fraud situation and the ones in the control group..



## ❖ Studies regarding fraud (cont.)

During the year of the fraud event, and in the 3 following years, the companies in fraud situation reduce slightly their executive board, reducing simultaneously their internal and external members; on the other hand, the companies in the control group increased slightly their executive board (but not significantly).

- **The authors conclude that the reduced impact from reported frauds in the study may reflect the favorable economic and financial characteristics for the period 1981-1992.**

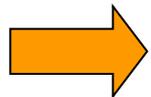


## ❖ Some books about corporate fraud

**Howard Schilit** published in 1993 the first edition of his book: “*Financial Shenanigans in 1993*”.

Criou um centro de análise e pesquisa (CFRA) para detectar precocemente sinais de aviso em relação a problemas operacionais ou “anomalias” contábilísticas. Na edição de **2002** do seu livro refere **30 técnicas** de “*tapeações*” financeiras definidas como práticas que distorcem intencionalmente a situação ou o desempenho financeiro reportado por uma empresa.

Em **2002** foi publicado por **Mulford e Comiskey** um livro semelhante com muitos outros exemplos.



These disclosures have caused outrage and resulted in **Sabanes-Oxley Act** (SOA) em 30 Julho de 2002.



## ❖ Sarbanes-Oxley Act

The **Sarbanes-Oxley Act** covers 11 main areas:

### 1. PCAOB – Public Company Accounting Oversight Board

PCAOB is a private nonprofit entity subjected to the regulation and supervision of the SEC.

This organization is responsible for the **supervision of the audit** listed companies and the establishment of standards for audit reports. All audit firms must be registered in the PCAOB.

All companies must report to its audit committee is composed of at least one member who is financial expert under the SEC definition.



## ❖ Sarbanes-Oxley Act (cont.)



### 2. Auditor independence:

- Audit firms are prohibited to providing non-audit services such as consulting
- The Audit Partner should rotate at least each 5 years.
- Audit reports should be directed to the audit committee rather than the management body.
- The auditing firm should not have employed an accounting or financial responsibility of the audited company during the period of one year before the audit.



## ❖ Sarbanes-Oxley Act (cont.)



**3. Certification:** The CEO and CFO must be sure that the report is according the SEC requirements and properly presents the financial position of the company (making false statements gives rise to a prison sentence between 10 and 20 years);

**4. Disclosures:** Each annual and quarterly report prepared in accordance with those norms SEC has to disclose all material off-balance-sheet transactions.

**5. Insider trading:** *Insider trading* with the stocks of the company in wich they work is considered an event subject to disclosure that must be reported in a *Form 4* *within a period of 2 days* (previously was until the 10th day of the month following the realization of the transaction).

**6. Conflict of interests:** Personal loans are prohibited by companies to administrators and directors;



## ❖ Sarbanes-Oxley Act (cont.)



**7. Professional responsibility:** New regulations will establish minimum standards of professional conduct regarding the lawyers who practice their activity in entities supervised by SEC.

**8. Studies and Reports:** Must be conducted several studies.

**9. Fraud accountability:** The elimination, alteration or falsification of registrations is a crime.

**10. Sanctions:** All audit or work papers must be kept for 5 years. False certifications or reports forgery must result in fines until 5 million dollar and/or prison until 20 years.

**11. Authority of SEC:** Everyone who had violated the antifraud norms may be prohibited of exercise administrative or management positions.



## ❖ NYSE

On August 16, 2002, the New York Stock Exchange (**NYSE**), submitted to the SEC for final approval a review of the **requirements for admission to listing**.



The new rules to admission the listing of shares in NYSE go beyond the auditor's independence conditions required by Sarbanes-Oxley Act.

The company must have an **audit commission** composed by at least 3 persons.

The commission must have a detailed description, in writing, about their activities.

The next slide details the **specifications for the independence of the board**:



## ❖ NYSE

### ❖ specifications for the independence of the board

- **Most members** of the board should be **independent**;
- The non-executive directors should meet regularly without the presence of executives;
- The boards must have independent **compensation committees** and **nomination committees**;
- All shareholders should vote on *stock options plans*;
- All listed companies must adopt a set of **guidelines** for **corporate governance**. Regarding the management guidelines, it should include their qualifications, responsibilities and compensation and access management;
- All listed companies must disclose a **code of conduct and ethics**.

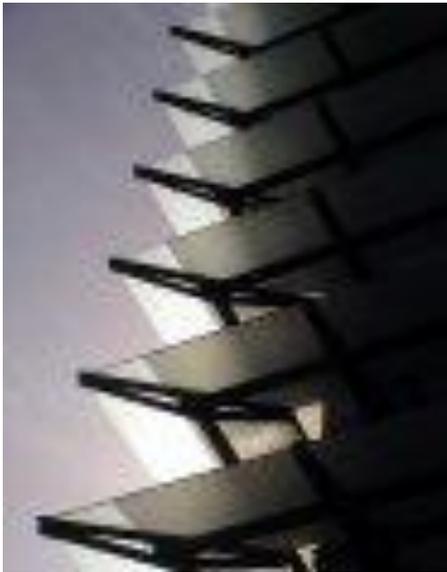


## ❖ Corporate Governance deficiencies

The **Sarbanes-Oxley Act** and the new requirements for listed stocks in NYSE focused the **deficiencies** perceived regarding **Corporate Governance**.

- The board members **were not independent**;
- The audit commission did not have enough independent management power;
- Audit firms had **conflicts of interests** resulting from providing non-audit services such as consulting
- CEO and CFO pursued an **aggressive accounting** and didn't assume any responsibility for the validity and security of financial reports;
- **Transactions** not reflected on the balance sheet **were not adequately disclosed**;
- **Personal loans** to directors were not justified;
- The **analysts' reports** suffered from **conflicts of interest**;
- The professional attitude of the **lawyers** did not check the minimum standards.
- The unlimited power of top executive allowed them to give themselves excessive bonuses and developed other ways of personal business

## ❖ Corporate Governance – an unfinished work



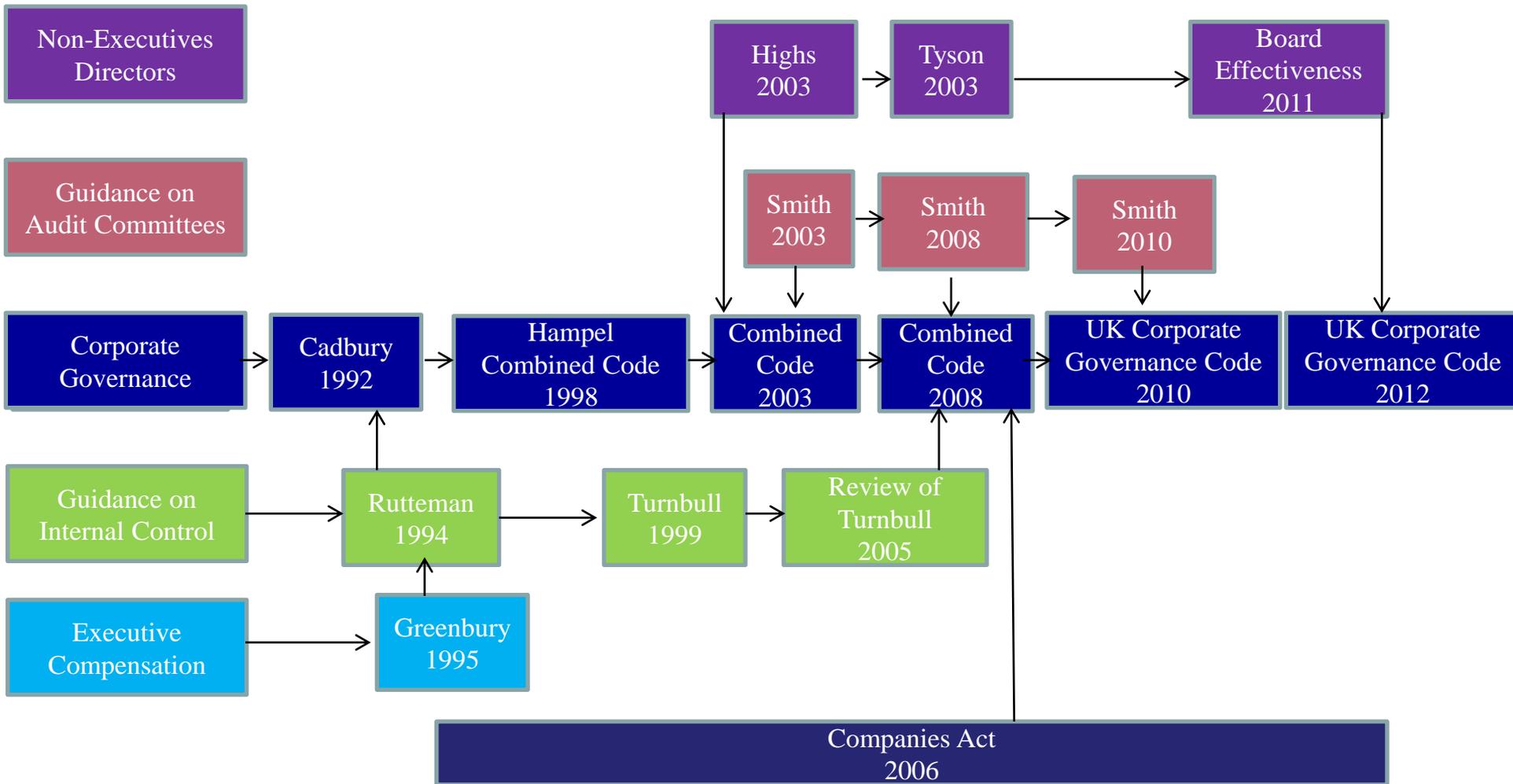
**It is not clear that the new laws and regulations corrected the faults of Corporate Governance.**

**This is indeed a work in progress.**

## **2. Legal and regulatory Guidelines concerning Corporate Governance in UK**



## UK Corporate Governance Timeline 1992-2012





## Other Relevant Codes and Reports

Association Investment  
Companies Code  
2003

Walker Report  
2009

Stewardship Code  
2010

### **Conclusion**

The UK corporate governance framework is constituted from a number of different sources, from formal legislation that must be strictly followed and can have high penalties for failure to do so, to the more principles based voluntary Combined Code. The framework ensures that basic standards of corporate governance are maintained throughout all companies incorporated in the UK whilst allowing flexibility to enable companies to implement corporate governance policies which fit their business model.

### **3. Legal and regulatory Guidelines and Models concerning Corporate Governance in Portugal**



### **3. Legal and regulatory Guidelines concerning Corporate Governance in Portugal**

The next slides will focused the legal and regulatory Guidelines concerning Corporate Governance in Portugal:



### 3. Legal and regulatory Guidelines concerning Corporate Governance in Portugal

#### OECD

The **OECD principles** on Corporate Governance state:

- It must be considered the denomination of **non-executive** members and **independent** members to the board.
- In the cases there are committees on the board, their duties and composition must be defined.
- The information about corporate governance policy must be disclosed.
- The **nomination and election** of the board must be a formal and transparent process.

#### Sarbanes-Oxley Act

Sarbanes-Oxley Act is mandatory for companies with listed stocks on the NYSE. It provides:

- Periodic evaluation of the effectiveness of the structure and internal control procedures
- Obligatoriness of an **audit committee** (at least one member has to be an expert in finance)

#### CMVM

The «**Regulamento CMVM 11/2003 – Governo das Sociedades Cotadas**» requires the board to distinguish between:

- **Executive** and **non-executive** members
- And **independent** and **non-independent** members

#### **CMVM November 2003 recommendation about Corporate Governance.**

- pelo menos **um membro** do órgão de administração deve ser **independente** (membro não associado a grupos de interesses específicos)
- members of the **remuneration committee** should be independent regarding the members of the Board

#### **«Regulamento da CMVM n.º 10/2005»**

- This regulation changes the regulations of **CMVM 7/2001** and **n.º 4/2004** for the Corporate Governance and Duties of Information.



### 3. Legal and regulatory Guidelines concerning Corporate Governance in Portugal

CSC	ISP	Community Directives
<p><b>CHAPTER VI - Administration, fiscalization and secretary of company</b></p> <p><b>SECTION I - Board of Directors</b></p> <p>Article 390.º - Composition</p> <p>Article 396. – Deposit</p> <p>Article 397.º - Transactions with company</p> <p>Article 399.º - Remuneration</p> <p>Article 405.º - Jurisdiction of the Board</p> <p><b>SECTION II - Fiscalization</b></p> <p><b>SECTION III – Audit Commission</b></p> <p><b>SECTION IV - Executive Board of Directors</b></p> <p><b>SECTION V - General and Supervisory Board</b></p> <p><b>SECTION VI - Statutory auditor</b></p> <p><b>SECTION VII –Company Secretary</b></p>	<p><b>Decree-Law 475/99</b> - It regulates the establishment and operation of pension funds and fund management companies. It defines:</p> <ul style="list-style-type: none"><li>• Responsible actuary(art. 32º)</li><li>• Management entity(art. 33º)</li><li>• Audit (art. 44º)</li><li>• Depositories(art. 51º)</li></ul> <p><b>Norm 21/2002-R</b> Política de investimento dos fundos de pensões. Define:</p> <ul style="list-style-type: none"><li>• The fund manager must define the process of recommendation, approval, implementation and monitoring of investment decisions</li></ul>	<p><b>The directive 2003/41/CE</b> concerning the activities and supervision of institutions for occupational retirement provision predicts:</p> <ul style="list-style-type: none"><li>• There must be <b>legal separation</b> between the company and institutions for managing occupational retirement provision (Article 8)</li><li>• The need of a <b>declaration of principles</b> regarding the <b>investment policy</b> that should be reviewed at least every 3 years.</li><li>• The Article 18 refers to the investment rules explaining in particular how to proceed in case of conflict of interest</li></ul>



### 3. Legal and regulatory Guidelines concerning Corporate Governance in Portugal

Year	Origin	Document	Recomendations Added
1986		Código das Sociedades Comerciais	<ul style="list-style-type: none"><li>* In Portugal the first legislation concerning corporate governance matters, even if not called by the name "Corporate Governance", appear in 1986 with the introduction of "Código das Sociedades Comerciais", that contained the basic rules on corporate management and control for all types of corporations.</li></ul>
1999	CMVM	Recommendations on Corporate Governance of Listed Companies	<ul style="list-style-type: none"><li>* Follow the OECD Principles of Corporate Governance, without imposing strict and uniform models. It mentioned topics such as disclosure of information, exercise of voting rights, shareholder representation, institutional investors, corporate rules and structure and functions of administration boards.</li></ul>
2001	CMVM	Recommendations on Corporate Governance of Listed Companies /CMVM Regulation No 7/2001	<ul style="list-style-type: none"><li>* Recomendations on the form of dutties regarding information disclosure on Corporate Governance pratices.</li><li>* Philosophy of comply or explain.</li></ul>
2003	CMVM	Recommendations on Corporate Governance of Listed Companies /CMVM Regulation No 11/2003	<ul style="list-style-type: none"><li>* Clarification of the concept of independent director.</li></ul>



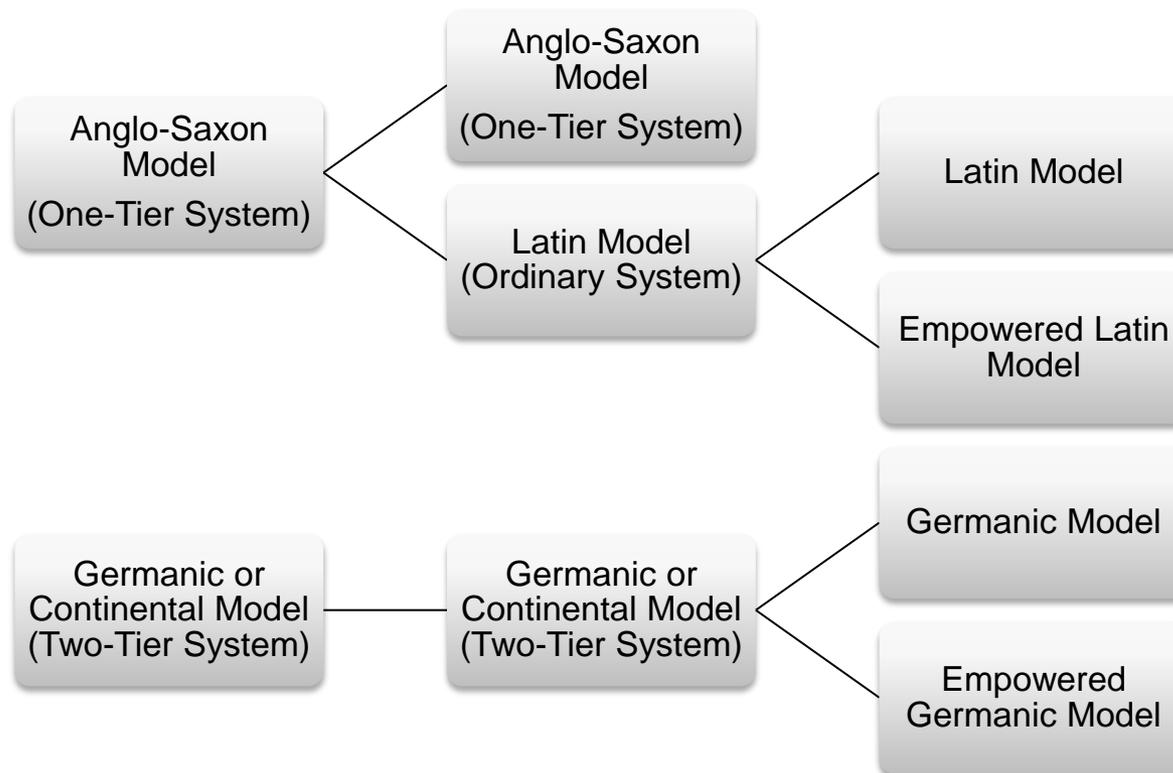
### 3. Legal and regulatory Guidelines concerning Corporate Governance in Portugal

Year	Origin	Document	Recomendations Added
2005	CMVM	Recommendations on Corporate Governance of Listed Companies /CMVM Regulation No 10/2005	<ul style="list-style-type: none"><li>* Internal supervisory mechanisms.</li><li>* Clarification of directors remuneration policies.</li></ul>
2006	IPCG	White Book on Corporate Governance	<ul style="list-style-type: none"><li>* Code of best practices.</li><li>* Summary of legal framework of corporate governance in Portugal, by identifying the different legal sources that originated the Portuguese codes.</li></ul>
2007	CMVM	Corporate Governance Code / CMVM Regulation No 1/2007	<ul style="list-style-type: none"><li>*43 recommendation grouped into 3 parts: General Meeting of Shareholders, Board of Directors and Supervisory Board, Information and Auditing.</li><li>*Dutties of transparency and information disclosure concerning directors.</li></ul>
2010	CMVM	Corporate Governance Code / CMVM Regulation No 1/2010	<ul style="list-style-type: none"><li>* Information disclosure on directors remuneration.</li><li>* Information disclosure on internal systems of corporate control and risk management.</li><li>* Independence of the External Statutory Auditor.</li></ul>



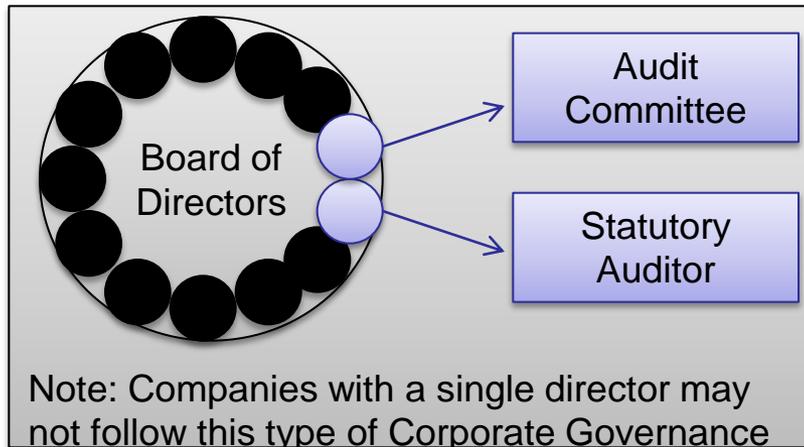
### 3. Corporate Governance Models in Portugal

The Portuguese legislation doesn't seek to impose strict or uniform Corporate Governance Models, instead it enables companies to choose between the following models (Article 278<sup>o</sup>, of *Código das Sociedades Comerciais*):



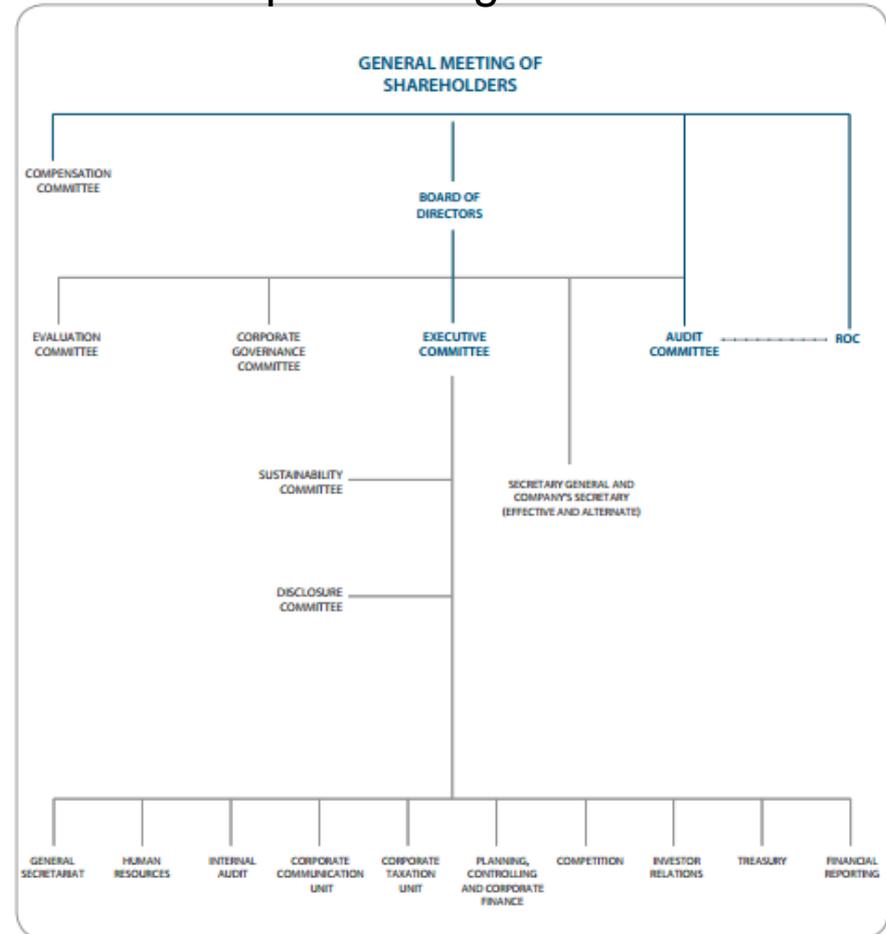
### 3. Anglo-Saxon Model (One-Tier System)

- Legal framework based in Anglo-Saxon countries (UK; USA; Canada; Australia);
- Market-oriented system, where an active external market for corporate control is used by independent shareholders to influence managerial decision-making;
- Individual shareholders play an important role with the principle “one share, one vote”.



Note: Companies with a single director may not follow this type of Corporate Governance Model.

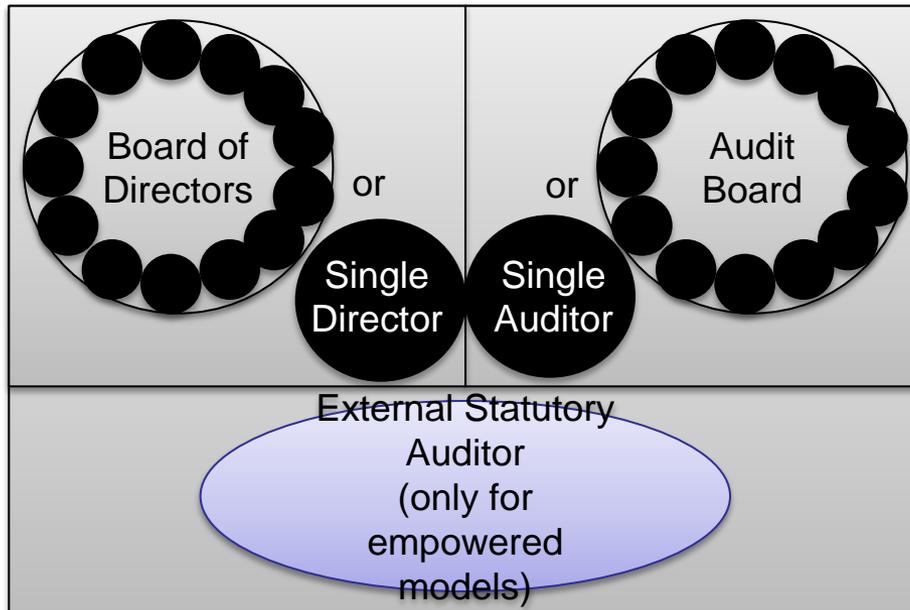
### Example: Portugal Telecom



Source: Portugal Telecom – Corporate Governance Report 2011.

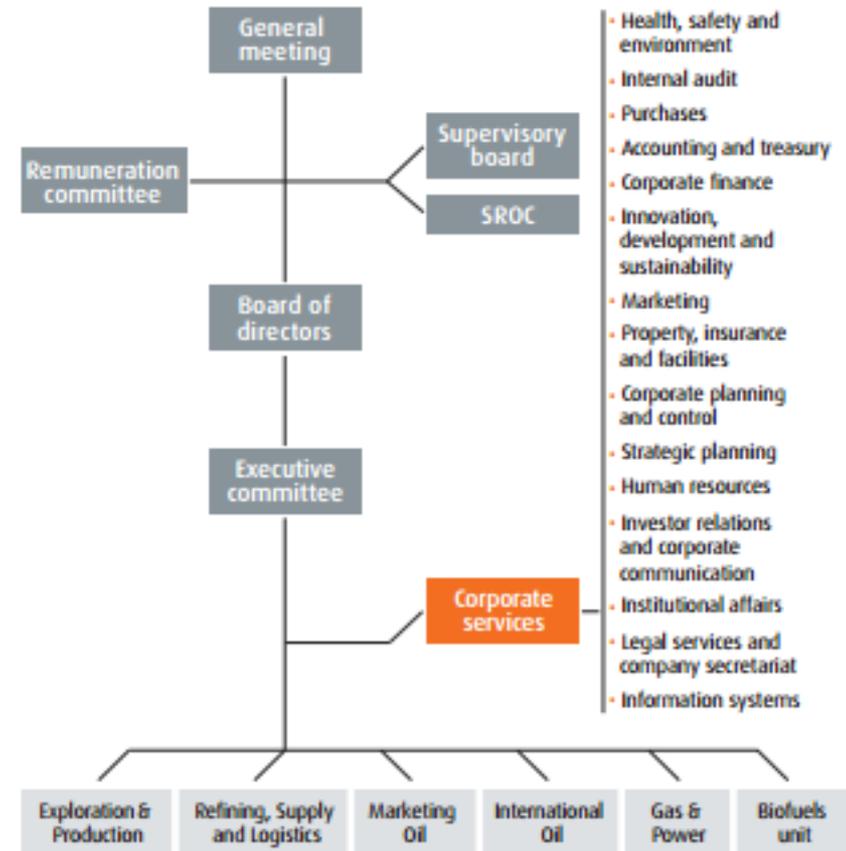
### 3. Latin Model (Ordinary System)

- Legal framework based in Latin countries (France; Italy; Spain; Portugal; ...);
- Network-oriented systems, where oligarchy groups sway managerial decision-making, by stable relationships.
- Relevant Shareholders (founding families; financial holdings; governments; firms with mutual cross-shareholdings) play an important role in management decisions.



### Example: Galp Energia

#### Galp Energia's governance structure

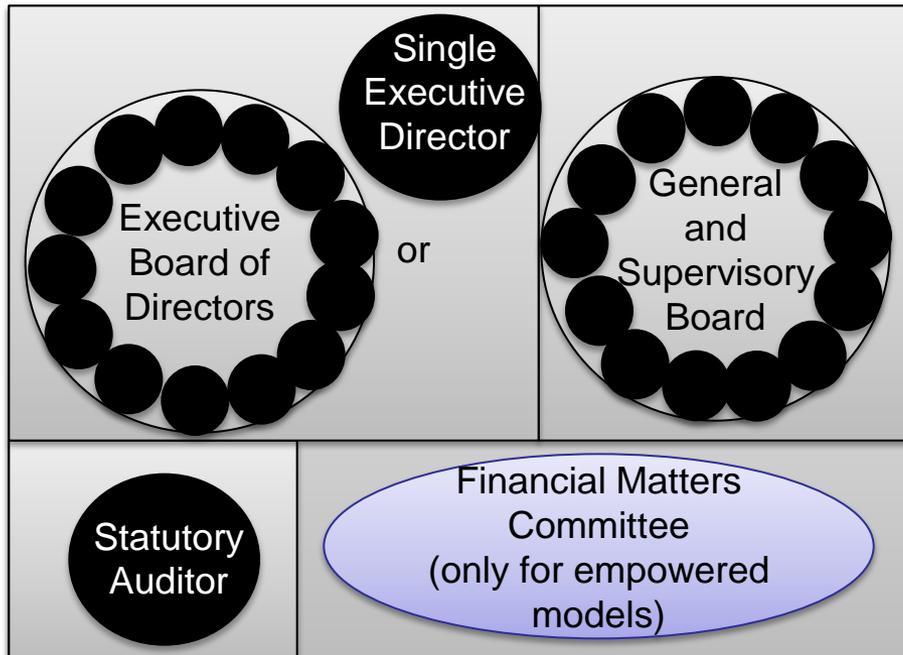


Source: Galp Energia – Corporate Governance Report 2011.



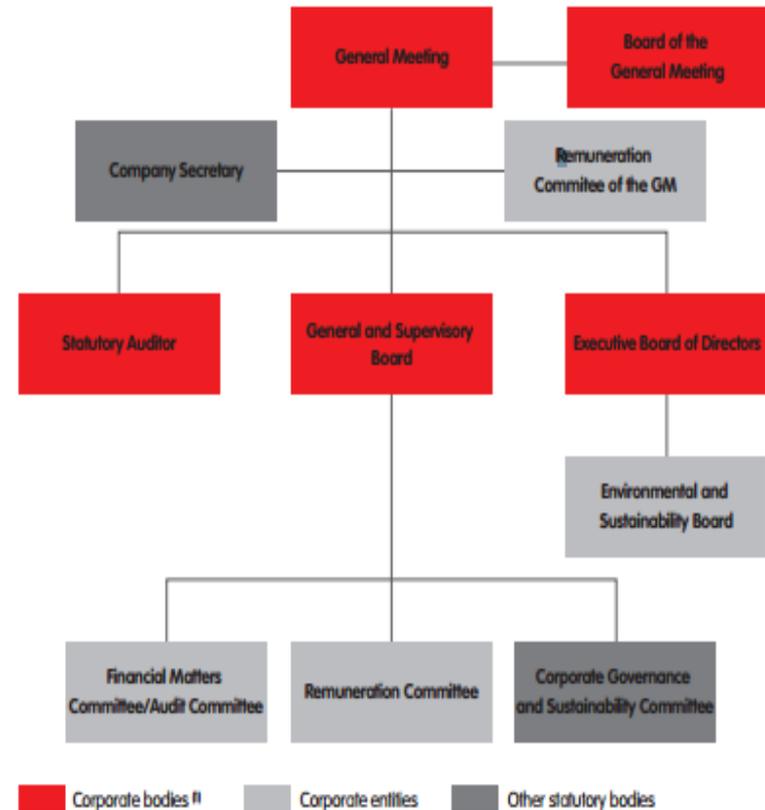
### 3. Germanic Model (Two-Tier System)

- Legal framework based in Germanic countries (Germany; Netherlands; Switzerland; Austria; ...);
- Network-oriented systems, where oligarchy groups sway managerial decision-making, by stable relationships.
- Relevant Stakeholders (relevant shareholders; corporate management; employees; suppliers; debt holders; firms with mutual cross-shareholdings) play an important role in management decisions.



### Example: EDP

#### ORGANIC CORPORATE STRUCTURE



# Corporate entities are also corporate bodies, pursuant to Article 8/4 of EDP's Articles of Association

Source: EDP - Annual Report 2011.

#### **4. Legal and regulatory Guidelines and Models concerning Corporate Governance in Germany**

## 4. Corporate Governance in Germany

- The task of the Supervisory Board is to advise regularly and supervise the Management Board in the management of the enterprise.

- The Supervisory Board appoints and dismisses the members of the Management Board.



- Responsible for independently managing in the interest of the enterprise, thus taking into account the interests of the shareholders, its employees and other stakeholders.



## 4. Corporate Governance in Germany

### Germanic Model

<b>Concept of the firm</b>	Institutional
<b>Board System</b>	<ul style="list-style-type: none"><li>• Two-Tier (management board and supervisory board)</li><li>• Management board is appointed and dismissed by the supervisory board, and supervisory board are appointed by the general assembly of shareholders</li></ul>
<b>Salient Stakeholders</b>	Industrial Banks, employees
<b>Importance of stock market in the national economy</b>	Stock markets play a small role



## 4. Corporate Governance in Germany

### Germanic Model

<b>Active external market control</b>	<ul style="list-style-type: none"><li>•Practically non-existent</li><li>•Mutual cross-shareholdings between firms are generally permitted and there is an implicit agreement that such shareholdings are not used to launch unwelcome takeovers</li></ul>
<b>Ownership concentration</b>	High ownership concentration
<b>Performance-dependent executive compensation</b>	Is not very common but is increasing recently
<b>Time horizon of economic relationships</b>	Long-term and stable economic relationships



## 4. German Corporate Governance Code

### Voting Cap:

- In principle, each share carries one vote. **There are no** shares with multiple voting rights, preferential voting rights (golden shares) or **maximum voting rights**.

### Independent Members:

- The Supervisory Board is responsible to decide what is an appropriate and reasonable number of independent members in the board.



## 4. German Corporate Governance Code

Compliance Degree:

- **‘Shall Recommendations’** which also reflect basic international governance standards. Companies that do not comply with these Recommendations have to state this in their annual report and/or their website.
- **‘Should Suggestions’** that represent additional international elements of good governance. These ‘Suggestions’ do not require an obligatory statement in case of non-compliance (but the Code encourages a detailed description of the application and any deviation from the ‘Suggestions’).



## 4. German Corporate Governance Code

Employee Ownership:

Employees have a participation on the company's stock

Employee Representation:

Employees have representatives in the board corresponding to:

- 1/3 of the board , if more than 500 employees
- 1/2 of the board if more than 2000 employees



## **5. Examples of Corporate Governance models**



## 5. Examples of Corporate Governance models

(the “two-tiered board” model)

### ❖ Allianz



In Germany the management and supervision is made by two different boards (two-tiered board):

**Board of Management** - is only responsible by managing the company: runs day-to-day operations.

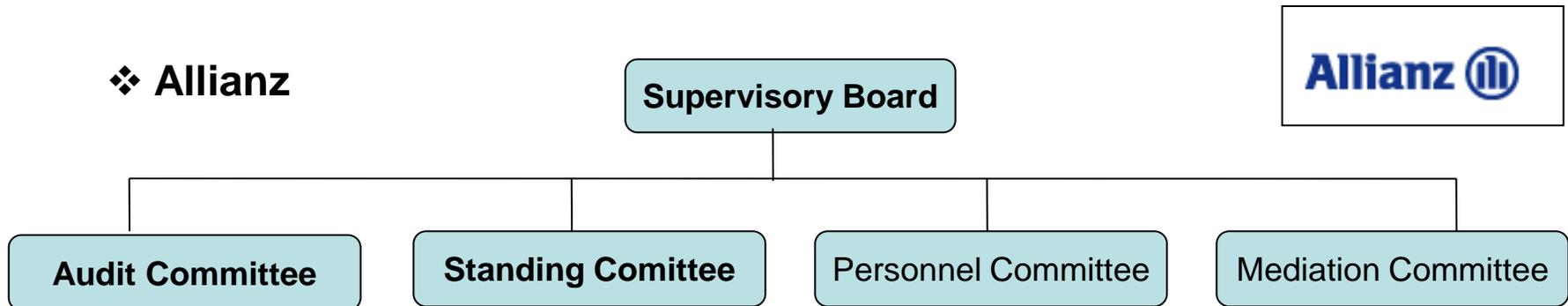
**Supervisory Board** - monitors and advises.

- The members of **Board of Management** are responsible by managing the company. Their functions are coordinated by the Chairman.
- The **Supervisory Board** is responsible by hire and fire the members of the management board, determine their compensation, and review major business decisions.



## 5. Examples of Corporate Governance models

### ❖ Allianz



#### Audit Committee

- 5 members (3 stockholders representatives and 2 employee representatives)
- 5 sessions in 2003
- It prepares Supervisory Board decisions regarding the approval of annual accounts;
- It analyzes the quarterly reports;
- It prepares the decision to appoint the auditor;
- It analyzes the auditor independence;
- It establishes the annual compensation for the annual audit;
- ...

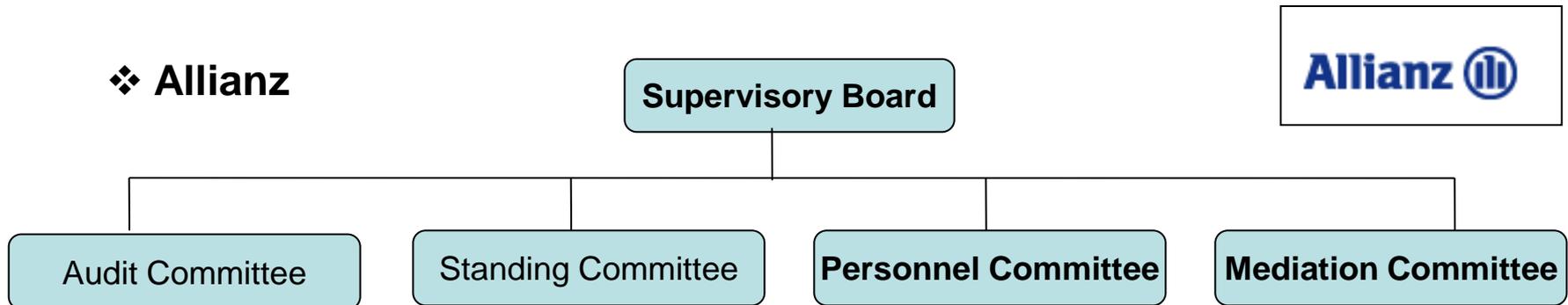
#### Standing Committee

- 5 members (2 employee representatives)
- It is responsible by approval of transactions that requires the approval of Supervisory Board, if the Supervisory Board chamber or other commission was not obligated to give that approval.



## 5. Examples of Corporate Governance models

### ❖ Allianz



#### Personnel Committee

- 3 members (Chairman of Supervisory Board, a stockholder representative and a employee representative in the supervisory board);
- It is responsible in particular for the preparation of the nomination / appointment of members of the Board of Management;
- Responsible for issues related to compensation remuneration

#### Mediation Committee

- According to German law, Mediation Committee has by function the resolution of conflict relating to the appointment of members of the Board of Management.
- Mediation Committee met only if the Supervisory Board do not get a two thirds vote ...



## 5. Examples of Corporate Governance models



### ❖ Axa

The Axa's corporate governance model compreende:

- **Supervisory Board**
- **Management Board**

**Supervisory Board** - monitors the operations of the company and reports to stockholders.

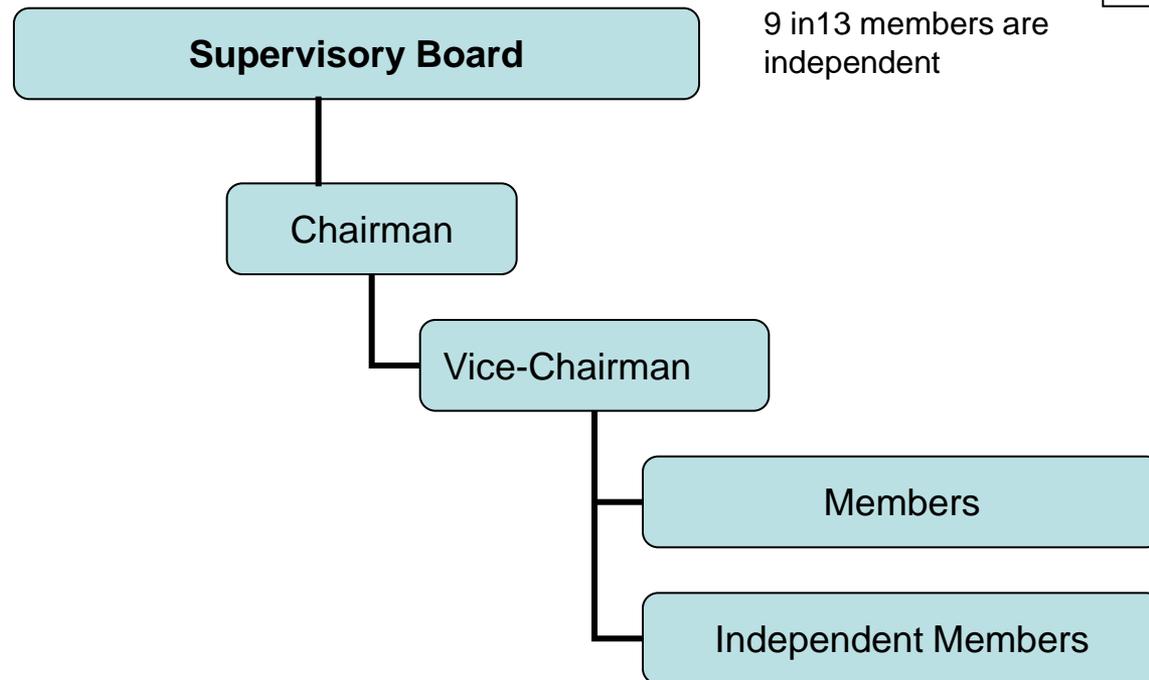
It appoints the Chairman and members of the Magament Board and supervises executive management.

Supervisory Board formally established “**Special Committees**” to help implementing the principles of Corporate Governance.

The Chairman and members are appointed by it as well as the specifications of their rights and duties.

## 5. Examples of Corporate Governance models

### ❖ Axa





## 5. Examples of Corporate Governance models

### ❖ Axa Special Committees

Supervisory  
Board



Audit Committee

Finance Committee

Selection & Governance  
Committee

Compensation  
Committee

#### Audit Committee

- 5 members (at least 1 of them has to be independent);
- 7 sessions in 2003;
- It examines the financial statements before they are presented to the Supervisory Board.
- It controls the nomination of external auditors of the company, approves the external audit programmes, results and recommendations as well as any actions taken in light of these recommendations.

#### Finance Committee

- 5 members (at least 1 of them has to be independent);
- 3 sessions in 2003;
- It examines and emits the recommendations about plans to sell properties or equity which amount of evaluation had exceeded the authorization given at Management Board by Supervisory Board;
- It reviews the major AXA's guidelines concerning the asset management politics and generally all related aspects with investment management policy.



## 5. Examples of Corporate Governance models

### ❖ Axa

#### Special Committees



Supervisory  
Board

Audit Committee

Finance Committee

Selection & Governance  
Committee

Compensation  
Committee

#### Selection & Governance Committee

- 5 members (at least 3 had to be independent);
- 2 sessions in 2003;
- It formulates recommendations to the Supervisory Board concerning the nomination of members to the Supervisory Board, special committees of Supervisory Board and the Management Board;
- The Committee is notified of the main meetings of top executives and directors of AXA.

#### Compensation Committee

- 5 members (at least 3 had to be independent);
- 5 sessions in 2003;
- It recommends the Supervisory Board compensation levels of the salary of the Management Board members, the amounts of fees payable to members of the Supervisory Board - subject to stockholder approval;
- Proposals for use of stock options to members of the Management Board.



## 5. Examples of Corporate Governance models

### ❖ Axa

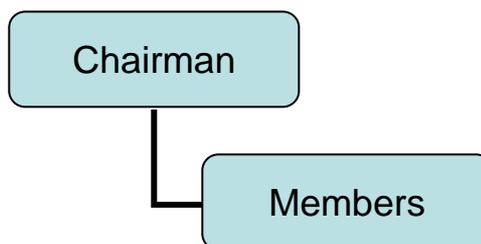


#### Management Board

Management Board is the decision-making body of AXA.

These members dedicate their time exclusively to managing the company.

Each member of Management Board has a specific responsibility about some concrete aspect in managing the company.





## 5. Examples of Corporate Governance models

(the “unitary system” model)

### ❖ Zurich



According to the company's social pact, the **Board of Directors** should have between **7 and 13 members**.

The members at Board of Directors are **non-executives**.

The Board of Directors should assemble at least 6 times per year.

The Board of Directors appointed the following committees that will report to it regularly and submit motions for resolutions.

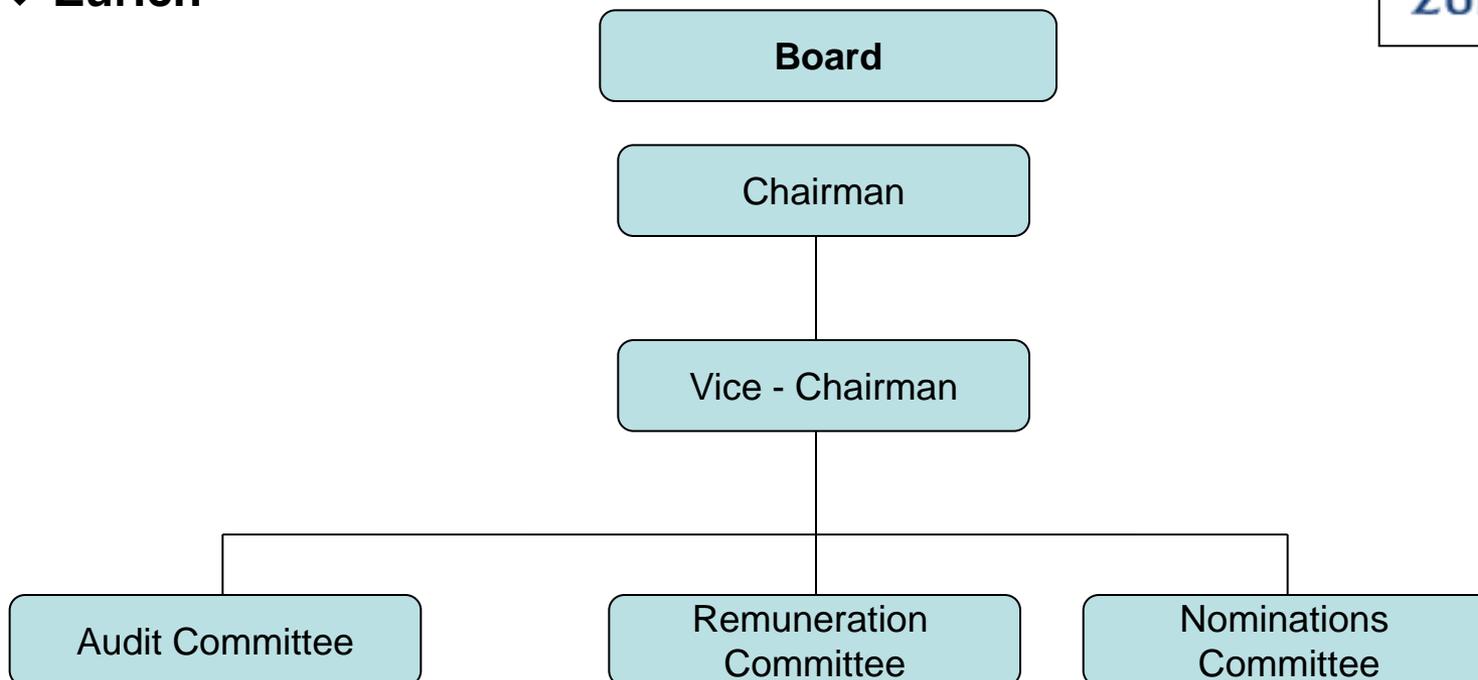
- **Remuneration committee**
- **Audit committee**
- **Nominations committee**



## 5. Examples of Corporate Governance models



### ❖ Zurich



## 5. Examples of Corporate Governance models

### ❖ Zurich



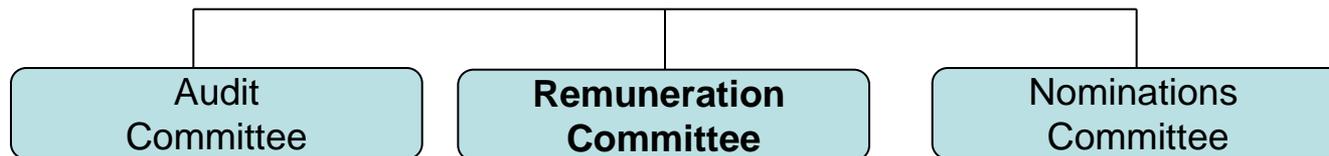
#### **Audit committee**

- It is composed by 5 members;
- Must assemble at least 4 times per year;
- It is the central organ to aspects of financial accounting, internal control, compliance and risk management between management, internal and external auditors;
- The Audit committee is responsible for reviewing the audit process of the company;
- It argues on daily basis with external auditors the accountants qualities and the group finances as well as any recommendation that the external auditors can have.
- Reviews the internal control systems.



## 5. Examples of Corporate Governance models

### ❖ Zurich



#### Remuneration committee

- It is composed by 6 members of the Board of directors.
- It should meet at least two times a year;
- It proposes to the Board of Directors the principles of remuneration for the Group and the remuneration of directors;
- It determines the metrics and performance analysis.



## 5. Examples of Corporate Governance models

### ❖ Zurich



#### **Nominations committee**

- It is composed by 5 members of the Board of directors;
- It should meet at least two times a year;
- It proposes the principles for the appointment and qualification of members to the Board of Directors;
- It shows proposals to Board of Directors about their composition, the nomination of Chairman and Vice-Chairman as well as CEO (the final decision however is taken by the Board of Directors).



## **6. Example of a Corporate Governance model for a portuguese company**

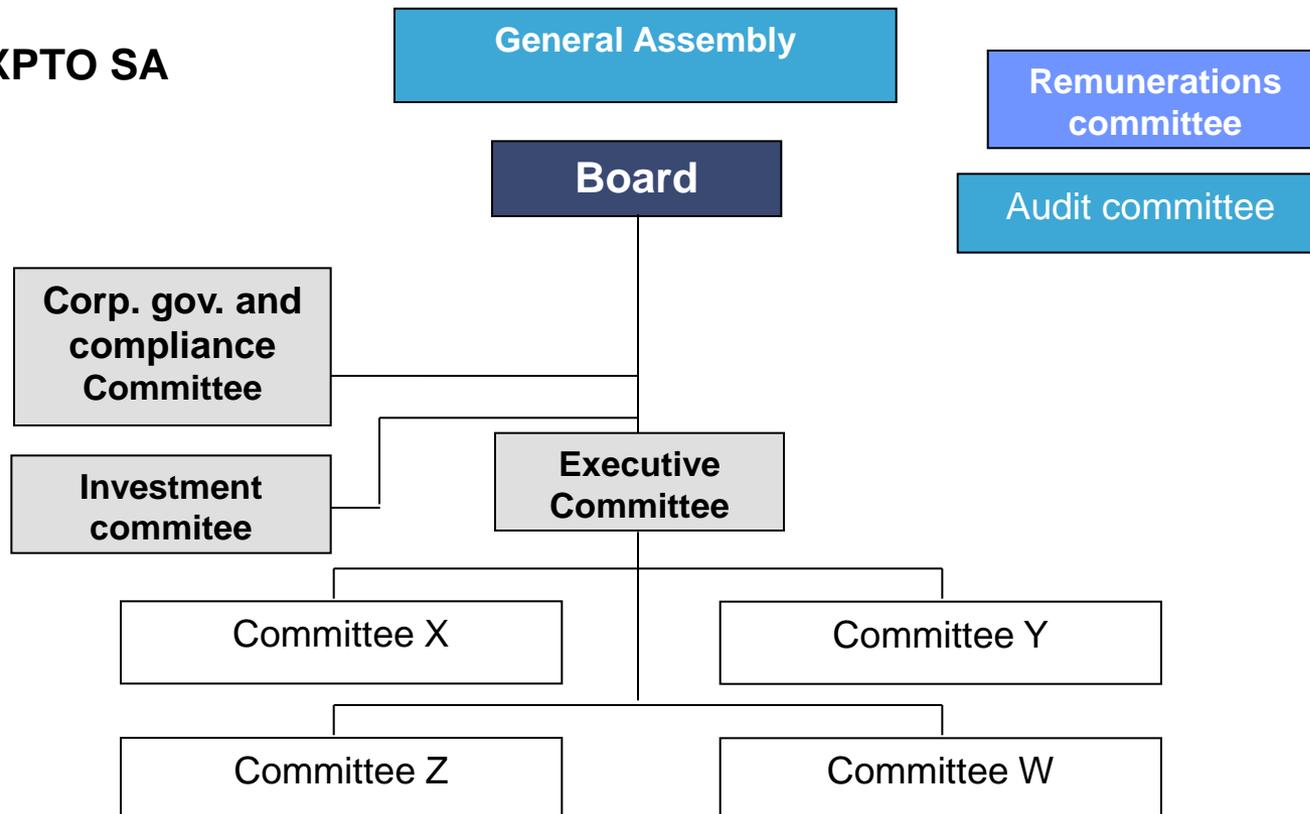


## 6. Example of a Corporate Governance model for a portuguese company

(the “unitary system” model – n.º1, al. a), art. 278º CSC)

**Latin Model**

**Company XPTO SA**





## 6. Example of a Corporate Governance model for a portuguese company

Composition of the Board:

		Chairman of the Board	Executive commission	Corp. gov. and conform. Commission	Comissão investimentos	total number of members
<b>Board</b>	<b>Executives Members</b>		3		1*	3*
	<b>Non-executives Members</b>	1		1	1	3
	<b>Independent non-executive Members</b>			1		1
		1	3	2	2	<b>7</b>
	<b>External Members</b>				2	2

(um dos membros é comum)



## 6. Example of a Corporate Governance model for a portuguese company

### Board

(art. 390º and following CSC)

### Functions

- Responsible for the overall management of the company

### Composition

- 3 non-executive members (one of which the CA's president)
- 3 executive members
- 1 independent member

### Assemblies \*

- 1 monthly meeting and whenever this is justified

### Year nomination

- 3 years



## 6. Example of a Corporate Governance model for a portuguese company

### Executive Committee

(nº3, art 407 CSC)

### Functions

- Responsible for leading the company's activities.

### Composition

- 3 executive members\*

### Assemblies

- 1 weekly meeting and whenever this is justified.

### Years nomination

- 3 years

\* **Note:** According nº 3, article 407 of CSC, the executive commission must necessarily be composed of an odd number of directors.



## 6. Example of a Corporate Governance model for a portuguese company

<b>Corp. gov. and compliance Committee</b>	<b>Composition</b>	<b>Assemblies</b>	<b>Years nomination</b>
<b>Functions</b>	<ul style="list-style-type: none"><li>• 1 non-executive member</li><li>• 1 independent non-executive member</li></ul>	<ul style="list-style-type: none"><li>• 1 quaterly meeting and whenever it is justified.</li></ul>	<ul style="list-style-type: none"><li>• 3 years</li></ul>
<ul style="list-style-type: none"><li>• Monitor and track conformity with the rules and regulations applicable to company's business</li><li>• Supervise the conformity with laws, regulations and statutes concernig corporate governance and discuss and approve measures to introduce or changes the observed principles and adopted procedures adopted by the company concerning its governance.</li><li>•Monitoring the effectiveness of corporate governance practices and make changes when necessary.</li></ul>			



## 6. Example of a Corporate Governance model for a portuguese company

<b>Corp. gov. and compliance Committee</b>	<b>Composition</b>	<b>Assemblies</b>	<b>Years nomination</b>
<b>Functions</b> <ul style="list-style-type: none"><li>• Monitor the continuing compliance with:<ul style="list-style-type: none"><li>• Separation functions</li><li>• Information mechanisms</li><li>• Control and risk management</li></ul></li><li>• Articulate with external auditors</li></ul>	<ul style="list-style-type: none"><li>• 1 non-executive member</li><li>• 1 independent non-executive member</li></ul>	<ul style="list-style-type: none"><li>• 1 quaterly meeting and whenever it is justified.</li></ul>	<ul style="list-style-type: none"><li>• 3 years</li></ul>



## 6. Example of a Corporate Governance model for a portuguese company

**Investment  
Committee**

**Functions**

**Composition**

- 1 executive member
- 1 non-executive member
- 2 external members

**Assemblies**

- 1 monthly meeting and whenever this is justified

**Years  
nomination**

- 3 years\*

- Responsible for the preparation of the written declaration of principles relating to investment policy (to prepare at least 3 in 3 years) - art. 12 of Directive 2003/41/EC
- Monitor the implementation of investment policies towards objectives and targets set
- Periodically send to the associated key information about the consultants and fund's sub-managers

\* **Note:** The external members may be appointed for a 2 or 3 years period.



## 6. Example of a Corporate Governance model for a portuguese company

**Remunerations  
committee**

**Functions**

**Composition**

• 3 shareholder members appointed by the general assembly and independent of the Board  
(art. 399<sup>o</sup> CSC; recomendation CMVM Nov. 2003)

**Assemblies**

• 2 annual meeting and whenever necessary

**Years  
nomination**

• 3 years

- Harmonize the remuneration of members of the board with the long-term interests of the company and its shareholders.
- Determine the total remuneration of each individual member of the Board of Directors, including, where appropriate, bonuses, incentive systems and options.
- Determine the targets to achieve the purpose of any remuneratory compensation based on performance.
- Be the only responsible for the establishment of selection criteria, effective selection and definition of terms of reference for any remuneration consultants who provide advice to the commission.



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## 7. Bibliography

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## APPENDIX 1

**Additional detail about the best practices regarding Corporate Governance**





## **Additional detail about the best practices regarding Corporate Governance**

- **OECD Principles of Corporate Governance**
- **Sarbanes-Oxley Act**
- **Código Sociedades Comerciais**
- **Regulations and recommendations CMVM**
- **European Commission**



## Additional detail about the best practices regarding Corporate Governance

### ❖ OECD Principles of Corporate Governance

It was approved in 1999 and since then the **OECD Principles of Corporate Governance** became an international reference. It provided a specific reference to the legislative and regulatory initiatives in both OECD member countries and other countries.

In 2004 there were a review of the principles as a result of accumulated experience, consultations with the private sector, workers, civil society and representatives of non-OECD countries.

- In this document OECD refers that there is **no single model of good corporate governance**



## Additional detail about the best practices regarding Corporate Governance

### ❖ OECD Principles of Corporate Governance

#### ▪ **Equitable treatment of shareholders**

- Corporate governance should ensure equitable treatment of all shareholders, including the minority ones

#### ▪ **Disclosure and transparency**

- Remuneration policy for members of the board and key executives
- Information about the members of the board, including their qualifications
- Independency
- Structures and government policies



## Additional detail about the best practices regarding Corporate Governance

### ❖ OECD Principles of Corporate Governance

#### ▪ Responsibilities of the Board

The board should:

- Set performance targets
- Oversee the implementation and company performance
- To ensure a formal and transparent process to **nominate** and elect the board
- To monitor and manage potential conflicts of interest between managers, members of the board and shareholders
- To harmonize the **remuneration** of top executives and members of the board with the long-term interests of the company and shareholders



## Additional detail about the best practices regarding Corporate Governance

### ❖ OECD Principles of Corporate Governance

#### ▪ Board Responsibilities

The Board should (cont.):

- To ensure the integrity of accounting and financial reporting, control risk, including the **independent audit**
- To exercise an objective and independent opinion on corporate business

To designate a sufficient number of **non-executive and independent** from board of directors capable of exercising an independent opinion about:

- Integrity of financial reporting and non-financial
- Analysis of transactions with related parties
- Appointment of members of the Board
- Remuneration of members of the board



## Additional detail about the best practices regarding Corporate Governance

### ❖ Sarbanes-Oxley Act

The Sarbanes-Oxley Act is mandatory for companies with securities listed on the New York Stock Exchange proposes, in particular:

- Management responsibility in establishing and maintaining adequate **internal control** structure and in the procedure for financial reporting.
- Periodic assessment of the structure effectiveness and internal control procedures for financial reporting purposes.

Sarbanes-Oxley Act provides the obligation of the existence of an **audit committee** with at least one member has to be an expert in finance.



## Additional detail about the best practices regarding Corporate Governance

### ❖ Código Sociedades Comerciais

#### Article 278 - Structure of management and supervision (in case of SA)

##### Chapter VI – Administration, fiscalization and secretary of company

###### **SECTION I - Board of Directors**

Article 390.º - Composition

Article 396. – Deposit

Article 397.º - Transactions with company

Article 399.º - Remuneration

Article 405.º - Jurisdiction of the Board

###### **SECTION II - Fiscalization**

###### **SECTION III – Audit Commission**

###### **SECTION IV - Executive Board of Directors**

###### **SECTION V - General and Supervisory Board**

###### **SECTION VI - Statutory auditor**

###### **SECTION VII – Company Secretary**



## Additional detail about the best practices regarding Corporate Governance

### ❖ Código Sociedades Comerciais

#### Article 278 - Structure of management and supervision (in case of SA)

1 The administration and supervision of the company can be structured according to **one of three modalities**: [Decreto-Lei n.º 76-A/2006, on March 29th]

- a) **Board of directors and supervisory board**; [Decreto-Lei n.º 76-A/2006, on March 29th]
- b) **Board of directors**, including an **audit committee** and **auditor**; [Decreto-Lei n.º 76-A/2006, on March 29th]
- c) **Executive board of directors, supervisory board and auditor**. [Decreto-Lei n.º 76-A/2006, on March 29th]



## Additional detail about the best practices regarding Corporate Governance

### ❖ Código Sociedades Comerciais

#### Article 278 - Structure of management and supervision (in case of SA)

2 - In cases prescribed by law, instead of the **executive board** or the **executive board of directors** may have **only one director** and instead of **council tax** can have a **single auditor**. [Decreto-Lei n.º 76-A/2006, on March 29th]

3 - In societies that have been structured according to the manner provided in subparagraph a), number 1, is mandatory, as provided by law, the **existence of a statutory auditor** who is **not a supervisory board member**. [Decreto-Lei n.º 76-A/2006, on March 29th]

4 - In societies that had been structured in accordance with the manner prescribed in paragraph c) above. 1, is mandatory, as provided by law, the existence of a **committee for financial matters in general and supervisory board** . [Decreto-Lei n.º 76-A/2006, on March 29th]

5 - **Companies with sole director** can not follow the manner provided in subparagraph b), number 1. [Decreto-Lei n.º 76-A/2006, on March 29th]

6 - At any time the contract can be modified to adopt other structure permitted by preceding paragraphs. [Previously number 3; Became number 6 by the Decreto-Lei n.º 76-A/2006, on March 29th]



## Additional detail about the best practices regarding Corporate Governance

### ❖ Código Sociedades Comerciais

#### Chapter VI – Administration, fiscalization and secretary of company

#### SECTION I - Board of Directors

#### Article 390.º - Composition

1- The board is composed by number of directors specified in the **contract of society**. [Decreto-Lei n.º 76-A/2006, on March 29th]



2 - The contract of society may stipulate that the company has only one director, provided that the **capital does not exceed EUR 200.000**; apply only to the administrator the provisions relating to the board that does not imply a plurality of administrators [Decreto-Lei n.º 343/98, on November 6th]

3 - The **administrators** may not be shareholders, but must be **individuals with full legal capacity**.



## Additional detail about the best practices regarding Corporate Governance

### ❖ Código Sociedades Comerciais

#### Chapter VI – Administration, fiscalization and secretary of company

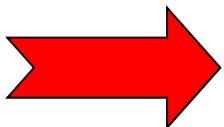
#### SECTION I - Board of Directors

#### Article 397.º - Business with the company

1 - It is forbidden to the company grant loans or credit to directors, make payments on their behalf, provide guarantees for liabilities incurred by them and give them advance payments of wages that exceed one month.

2 - Are **null the contracts between the company and its directors**, directly or through an intermediary, if not previously authorized by resolution of the board, in which the person concerned can not vote, and with the favorable opinion of the council tax [Decreto-Lei n.º 76-A/2006, on March 29th]

4 In its **annual report**, the board shall **specify the authorizations** it has **granted under number 2** and the **report of the supervisory board or audit committee** shall include the opinions delivered on those authorizations. [Decreto-Lei n.º 76-A/2006, on March 29th]





## Additional detail about the best practices regarding Corporate Governance

### ❖ Código Sociedades Comerciais

#### Chapter VI – Administration, fiscalization and secretary of company

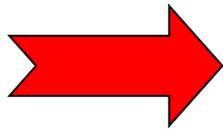
#### SECTION I - Board of Directors

#### Article 399.º - Remuneration

1 It's the competence of the **general meeting of shareholders** or a **committee** nominated by it set the **remuneration** of each director, taking into account the functions performed and the **company's economic situation**. [Decreto-Lei n.º 76-A/2006, on March 29th]

2 - The remuneration may be fixed or partially include a **percentage of the profits of exercise**, but the **maximum percentage** for board members must be **authorized by a provision of the partnership contract**. [Decreto-Lei n.º 76-A/2006, on March 29th]

3 - The percentage mentioned in the preceding paragraph does not affect the distribution of reserves or any part of profit which could not, by law, be distributed to shareholders.





## Additional detail about the best practices regarding Corporate Governance

### ❖ Código Sociedades Comerciais

#### Chapter VI – Administration, fiscalization and secretary of company

#### SECTION II - Fiscalization

#### Article 413 - Structure and quantitative composition

- 1 - **The audit of companies** adopting the manner provided for in subparagraph a) of number 1 of Article 278 has as a responsible:[Decreto-Lei n.º 76-A/2006, on March 29th]
  - a) An **auditor**, which must be statutory auditor or a **firm of statutory auditors**, or a **supervisory board**; [Decreto-Lei n.º 76-A/2006, on March 29th]
  - b) A **supervisory board** and an **statutory auditor** or a **firm of statutory auditors not being a member of that body**. [Decreto-Lei n.º 76-A/2006, on March 29th]



## Additional detail about the best practices regarding Corporate Governance

### ❖ Código Sociedades Comerciais

#### Chapter VI – Administration, fiscalization and secretary of company

##### SECTION II - Fiscalization

#### Article 413 - Structure and quantitative composition

3 - The **auditor** will always have an **alternate** who is also a **statutory auditor or firm of statutory auditors**. [Previous number 2; passed to number 3 by Decreto-Lei n.º 76-A/2006, on March 29th]

4 - The **supervisory board** is composed by the number of members fixed in the statutes, with a **minimum of three members**. [Decreto-Lei n.º 76-A/2006, on March 29th]

5 - Being three the members of the supervisory board, there must be one or two alternates, having always two alternates when the number of members were greater than three. [Decreto-Lei n.º 76-A/2006, on March 29th]

6 - The **auditor** shall be governed by the **laws** relating to the a **statutory auditor** and additionally, where applicable, the provisions regarding the supervisory board and its members. [Decreto-Lei n.º 76-A/2006, on March 29th]



## Additional detail about the best practices regarding Corporate Governance

### ❖ Código Sociedades Comerciais

#### Chapter VI – Administration, fiscalization and secretary of company

#### SECTION III – Audit Committee

#### Article 423-B - Composition of the audit committee

- 1 - The **audit committee** referred to in subparagraph b) of number 1 of Article 278 is an organ of a society composed by **part of the board members**.
- 2 - The audit committee is composed by the **number of members fixed in the statutes, a minimum of three members**.
- 3 - To the **members of the audit committee** is sealed the exercise of executive functions in society and is applicable to them Article 414 A, with the necessary adjustments, except as provided in subparagraph b) of number 1 of the same article.



## Additional detail about the best practices regarding Corporate Governance

### ❖ Código Sociedades Comerciais

#### Chapter VI – Administration, fiscalization and secretary of company

#### SECTION III – Audit Committee

#### Article 423-B - Composition of the audit committee (cont.)

4 - In the companies that issue securities admitted to trading on regulated markets and societies that meet the **criteria** referred to in subparagraph a) of **number 2** of Article **413**, the **audit committee** must **include** at least one member who has higher education appropriate to the exercise of their functions and knowledge of auditing or accounting and who, under number 5 of Article 414, should be independent.

5 -In companies whose shares are admitted to trading on a regulated market, members of the audit committee should, in their majority, be independent.

6 - It is applicable number 3 of Article 414



## Additional detail about the best practices regarding Corporate Governance

### ❖ Código Sociedades Comerciais

#### Chapter VI – Administration, fiscalization and secretary of company

#### SECTION IV - Executive Board of Directors

#### Article 424 - Composition of the Executive Board of Directors

1 - The **executive board of directors**, referred to in subparagraph c) of number 1 of Article 278, is composed of the **number of directors prescribed in the statutes**. [Decreto-Lei n.º 76-A/2006, on March 29th]

2 - A company may have a **single administrator** if their **capital does not exceed € 200,000**. [Decreto-Lei n.º 76-A/2006, on March 29th]



## Additional detail about the best practices regarding Corporate Governance

### ❖ Código Sociedades Comerciais

#### Chapter VI – Administration, fiscalization and secretary of company

#### SECTION V - General and Supervisory Board

#### Article 434 - Composition the general and supervision board

1 - The **general and supervision board**, with regard to subparagraph c) of number 1 of Article 278, is composed of the number of members specified in the contract of society, but always greater than the number of directors. [Decreto-Lei n.º 76-A/2006, on March 29th] [Corrected by the Declaração de Rectificação n.º 28-A/2006, on May 26th]

2 – [extinct by the Decreto-Lei n.º 76-A/2006, on March 29th]

3 - Applies the provisions of the second part of number 3 and numbers 4 and 5 of Article 390

4 - For the composition of the general and supervision board shall apply numbers 4 to 6 of Article 414 and Article 414-A, with the exception of subparagraph f) of number 1 of this latter article, except as regards the commission provided in number 2 of Article 444. [Added by the Decreto-Lei n.º 76-A/2006, on March 29th] [Corrected by the Declaração de Rectificação n.º 28-A/2006, on May 26th]



## Additional detail about the best practices regarding Corporate Governance

### ❖ Código Sociedades Comerciais

#### Chapter VI – Administration, fiscalization and secretary of company

#### SECTION V - General and Supervisory Board

#### Article 434 - Composition the general and supervision board

5 - In the absence of authorization by the General Assembly, members of the general and supervision board can not exercise on their own or others' business competitor of the company neither hold office in a competing company. [Added by the Decreto-Lei n.º 76-A/2006, on March 29th]

6 - The authorization referred to in the preceding number shall define the rules governing access to sensitive information by the board member. [Added by the Decreto-Lei n.º 76-A/2006, on March 29th]

7 - For the purposes of the requirements in numbers 4 and 5, it's applied the provisions in numbers 2, 5 and 6 of Article 254. [Added by the Decreto-Lei n.º 76-A/2006, on March 29th]



## Additional detail about the best practices regarding Corporate Governance

### ❖ Código Sociedades Comerciais

#### Chapter VI – Administration, fiscalization and secretary of company

#### SECTION VI - Statutory auditor

#### Article 446 - Designation

1 - In companies with the structures referred to in **subparagraphs b) and c)** of number 1 of Article 278 or the structure referred to in subparagraph b) of number 1 of Article 413 on a proposal from audit committee the general and supervisory board, from the commission for financial matters or from the **supervisory board**, the general meeting shall appoint an **auditor** or a firm of auditors to **inspect the accounts of the society**. [Decreto-Lei n.º 76-A/2006, on March 29th]

2 - The designation is made for a **period not greater than four years**. [Decreto-Lei n.º 76-A/2006, on March 29th]

3 - The auditor shall perform the duties provided for in subparagraphs c), d) e) f) of number 1 of Article 420 [Decreto-Lei n.º 76-A/2006, on March 29th]



## Additional detail about the best practices regarding Corporate Governance

### ❖ Código Sociedades Comerciais

#### Chapter VI – Administration, fiscalization and secretary of company

#### SECTION VII – Company Secretary

#### Article 446-A - Designation

- 1 - The issuers of **shares listed to the negotiation** on a regulated market must appoint a **company secretary and a substitute**. [Decreto-Lei n.º 76-A/2006, on March 29th]
- 2 - The **secretary and his substitute** should be **appointed by the partners** in the act setting up the company or by the board of directors or by the executive board of directors by resolution recorded in the minutes. [Decreto-Lei n.º 76-A/2006, on March 29th]
- 3 - The function of secretary shall be performed by people with higher education appropriate to the performance of functions or solicitor, however it can not exercise them in more than seven companies, except in that in the situations provided for in Title VI of the Code.
- 4 - In case of absence or disability of the Secretary, its functions are exercised by his substitute



## Additional detail about the best practices regarding Corporate Governance

### ❖ CMVM

#### Regulamento CMVM 11/2003 – Governo das Sociedades Cotadas

requires the board to distinguish between:

- **executive** and **non-executive** members
- and **independent** and **non-independent** members
  
- If there is an **executive committee** or **other committees**:
  - identification of the **powers** and competences allocated to these committees and their **composition and indication of directors considered independent** (in accordance with number 2 of Article 1)
  - indication of the number of the board meetings



## Additional detail about the best practices regarding Corporate Governance

### ❖ CMVM

#### CMVM Recommendation in November 2003 on the Government Companies

- suggests that at least **one member** of the management body be **independent** (not-associated member with specific interest groups) (Chapter IV, number 6)
- the board of directors should **create internal control committees** with powers to **assess the structure and corporate governance** (Chapter IV, number 7)
- members of the **remuneration committee** should be **independent** in relation to members of the board (Chapter IV, number 9)



## Additional detail about the best practices regarding Corporate Governance

### ❖ CMVM

#### Regulamento da CMVM n.º 10/2005

- amending CMVM Regulations in 7/2001 and number 4/2004 concerning the Corporate Governance and the Obligations of Information

The changes recommended by CMVM Regulation number 10/2005 had as main objectives:

- Strengthen the surveillance system (checks and balances) within the company
- Enhance transparency
- Adapt the interim information to the Standards IAS / IFRS



## Additional detail about the best practices regarding Corporate Governance

### ❖ CMVM

#### Regulamento da CMVM n.º 10/2005

- The **strengthening of the supervision system** is realized by adopting a more demanding concept of independence, incorporating a functional element besides the well-established relational element, and centralized now in the figure of the non-executive director, the context more conducive to the exercise of functions assigned to an independent member of the Board.
- This regulatory intervention also promoted a **greater transparency** in three areas whose relevance it is accentuating recently: **remuneration of directors policy, communication of improprieties and qualifications of directors**, leading to changes in higher-level information requirements of the Annual Report About Corporate Governance.
- With regard to **financial information**, were established a minimum framework for reference IAS / IFRS on the financial information of the first and third quarter but without forcing a quarterly financial report, therefore do not apply the IAS 34.



## Additional detail about the best practices regarding Corporate Governance

### ❖ European Commission

**European Commission Recommendation n. ° 2005/162/EC** of 15 February 2005 on the Role of Non-Executive Directors and

**European Commission Recommendation n. ° 2004/913/EC** of 14 December 2004 on the Remuneration of Directors.



## ***Exercise***

***New model of corporate  
governance in a post-  
acquisition operation***



## Exercise

Company Alfa S.A. dedicates to manufacturing (laser cutting) and commercialization of steel components for different industries, in particular the automotive industry. This company was formed about 10 years ago and has always been owned in two equal parts of 50% for each of its two managing partners. Your company, the acquiring company, just acquired 60% of the share capital of that company. Your company is one of the leading companies in the steel sector in Portugal with a very strong financial capacity. The acquiring company is a family business in which the management is done by the parents and two sons (all with a university degree in management).

### **It is intended to:**

Submit a suggestion concerning the Corporate Governance model that may be adopted in the post-acquisition of Alfa S.A.



Telmo Francisco Vieira

[tfv@iseg.utl.pt](mailto:tfv@iseg.utl.pt)

[telmo.fv@gmail.com](mailto:telmo.fv@gmail.com)

Mobile + 351 917 820 650