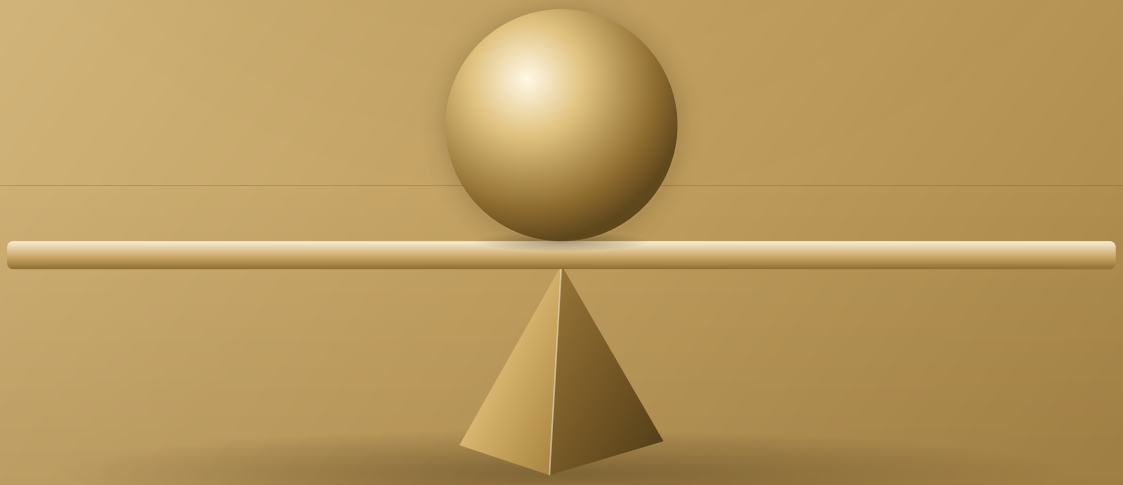
BICG

BALTIC INSTITUTE OF
CORPORATE GOVERNANCE



HANDBOOK FOR BALTIC BOARDS AND BUSINESSES

CORPORATE GOVERNANCE IN PRACTICE FOR BOARDS, OWNERS AND MANAGERS

2026

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FOREWORD

Sara Sultan
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THE ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT (OECD)

“

Translating corporate governance principles into effective practice is where governance delivers value. The G20/OECD Principles of Corporate Governance and the OECD Guidelines on Corporate Governance of State-Owned Enterprises provide internationally agreed standards and recommendations, but their effectiveness ultimately depends on how they are understood and applied in the specific circumstances in which companies operate.

Practical resources such as this Handbook can play an important role in supporting boards, shareholders and governance practitioners in navigating increasingly complex responsibilities. Its attention to the corporate governance environment of the Baltic region is particularly valuable, while addressing issues relevant across different ownership structures, including privately owned, listed and state-owned enterprises.

Strong corporate governance supports informed and accountable decision making, effective oversight and sustainable value creation over the long term. By encouraging continued reflection on how good governance principles can be put into practice, the Baltic Institute of Corporate Governance contributes to the broader dialogue on strengthening corporate governance standards and practices in the region.

ENDORSEMENTS

Arminta Saladžienė

Vice President

European Markets

NASDAQ

“

Over the recent decades, Baltic businesses have grown from entrepreneurial ventures into regional leaders and international champions, creating immense value while operating in an increasingly complex environment. As companies grow, so do their risks. Markets expand, organizations become more sophisticated, technologies evolve, and stakeholder expectations rise. The fundamental challenge of governance is ensuring that steering and oversight keep pace with risk. Governance failures rarely occur because organizations take risks; they occur when risks outgrow an organization's ability to understand, challenge, and oversee them. Good governance is therefore not a one-size-fits-all formula but a matter of proportionate, risk-based judgment.

This Handbook is a unique contribution to that effort. Comprehensive in scope yet practical in application, it addresses every major dimension of governance and is relevant not only for listed companies, but also for private, family-owned, founder-led, and state-owned enterprises, making it valuable for founders, shareholders, Board members, executives, governance professionals, and policymakers alike.

By bringing together the full spectrum of modern governance in a single volume, the Baltic Institute of Corporate Governance once again demonstrates its leadership in raising standards not only across the Baltics, but throughout Europe.

Maria Pierdicchi

Chair of the Board

EUROPEAN CONFEDERATION OF DIRECTORS' ASSOCIATIONS (ECODA)

"

This Handbook gives key insights to good corporate governance with a holistic approach. It provides good guidelines and pragmatic suggestions on how the decision-making process by the Boards can be made effective, rigorous and based on solid governance principles.

Good governance practices are essential in enabling companies to be more competitive by helping to separate ownership from management and effectively bring together independent perspectives, while ensuring accountability. It improves resilience by introducing adequate controls, risk governance and conflict resolutions. Ultimately, it improves value creation over time by unifying long term sustainable strategies with economic success - for the benefits of both shareholders and stakeholders.

And Europe needs to continue to strengthen its corporate governance practices, with National Director Institutes having an important role to play in providing the best tools and trainings among complex challenges affecting all companies.

The Handbook produced by the Baltic Institute of the Corporate Governance is a very useful tool to support the work of all Boards in the current context.

I hope this very complete work will support the Baltic region in its growth and prosperity, by encouraging adoption of strong corporate governance practices across all companies as a key success factor.

ACKNOWLEDGEMENTS

This Handbook is the result of four years of collective effort by members of the Baltic Institute of Corporate Governance (BICG). It unifies the knowledge and practical experience of Board members and Chairs, corporate secretaries, in-house counsel, legal advisers and other corporate governance professionals, who deal with governance questions daily, be it in private businesses, listed companies, state- and municipality-owned enterprises or company groups.

BICG is grateful to the co-authors for their commitment, professionalism and generosity with their time and knowledge. Over many working sessions, drafts and reviews, they shaped the Handbook's structure, drafted and challenged its content, and made sure that its recommendations reflect how Boards in the Baltics can and should actually work.

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Positions are given as at the time of publication. Brief biographies of the co-authors are available in the section "About the authors".

The co-authors contributed in their personal expert capacity and the Handbook was not co-ordinated with the organisations they represent. Dependability of the content rests solely with the BICG.

We are also grateful to the members of the BICG Policy Group Latvia for their thoughtful expert comments during the review of the Handbook.

Finally, special thanks go to the entire team of the BICG, whose coordination made this project possible.

INTRODUCTION

Good corporate governance is essential for creating strong, resilient and trusted businesses. It defines how companies are led, controlled and held accountable, and how the roles of shareholders, the Board, management and other stakeholders are organised in practice. It is about better decision-making, clearer responsibilities, effective oversight, competent leadership and sustainable long-term value creation.

This Handbook has been prepared keeping in mind the businesses operating in the three Baltic countries of Estonia, Latvia and Lithuania. It reflects the governance context of the region, where companies often operate with concentrated ownership, in developing capital markets and have a need for more professional Boards as well as better overall corporate governance practices. At the same time, many of the principles and recommendations included here are universal. Therefore, the Handbook will be useful to companies, Board members, shareholders, executives, advisers, policy makers and other governance practitioners outside of the Baltics as well.

The purpose of the Handbook is to provide a highly practical guidance on how good corporate governance can be applied in real companies. It does not seek to replace national laws, stock exchange rules, sector-specific regulations, company statutes or professional legal advice. Instead, it should be used as a reference point and practical tool for improving Board work, shareholder relations, management accountability, strategic direction, risk oversight, internal controls, disclosure and ethics, helping to ensure long-term success of an enterprise.

The Handbook is based on internationally recognised corporate governance standards and good practices, including guidance by the Organisation for Economic Co-operation and Development (OECD), recommendations by the European Confederation of Directors' Associations (ecoDa) and other widely respected governance organisations. But while these sources provide an important benchmark, the Handbook goes further and adapts their principles to the practical needs of a businesses.

It is also important to note that a key principle of this Handbook is proportionality (i.e. “one size does not fit all”). Not every company needs the same governance structure. A listed company, a private enterprise, a family business, a state-owned enterprise and a subsidiary in a group will likely apply governance practices differently. However, all companies benefit from clear separation of leadership roles, competent and independent oversight and a long-term view towards value creation.

IMPORTANT NOTICE – DISCLAIMER

This Handbook reflects established international best practices in corporate governance. It is intended as practical guidance only and does not constitute legal advice. It does not supersede, replace, or limit any applicable national mandatory legislation, regulatory requirements, or binding rules of any stock exchange or supervisory authority.

In all circumstances, a company and its Board must comply with the laws and regulations of each country in which the company operates. Where national legislation or regulation prescribes a different approach from that recommended in this Handbook, the applicable mandatory legal requirements must be followed. Companies operating in multiple jurisdictions should seek qualified local legal counsel to ensure full compliance with all relevant rules.

This Handbook was prepared with the assistance of artificial intelligence tools, which supported research, drafting, and synthesis of relevant international frameworks and best practices. All content has been reviewed and validated by subject-matter experts. It should not be relied upon as a substitute for professional legal, financial, or governance advice tailored to a company's specific situation.

HOW TO USE THIS HANDBOOK

This Handbook is designed to be used as a **practical working document**. Readers do not need to read it only from beginning to end. Individual chapters may be used separately, depending on the needs of the company, the Board, shareholders or management.

Boards may use the Handbook to review their roles, responsibilities, agenda planning, committee structure, evaluation process, information flows and relationship with management. Board chairs may use it to improve Board effectiveness, meeting quality, decision-making and Boardroom culture. Shareholders may use it to better understand their rights, responsibilities and interaction with the Board. Management teams may use it to clarify expectations from the Board and to strengthen reporting, internal control, risk management and execution of strategy.

Companies may also use the Handbook as a self-assessment tool. Each chapter can serve as a basis for discussion: does our company follow this principle; is our current practice proportionate to our size, ownership structure and risks; what should be improved; and who is responsible for the next step? The Handbook may also support induction of new Board members, preparation of Board charters, review of governance policies, shareholder discussions and Board training.

This Handbook should not be treated as a rigid checklist. Good governance requires judgement. The right governance solution depends on the company's legal form, ownership model, stage of development, complexity, regulatory environment, stakeholder expectations and public-interest profile. The aim is not to copy formal structures, but to build governance arrangements that work in practice and improve the quality of decisions in particular company in specific time period.

> The Handbook is intended to be **a "live" document**. Corporate governance standards continue to develop, and the expectations of investors, regulators, owners and society are changing. BICG may update the Handbook, or individual chapters of it, whenever necessary. This may happen, for example, when the OECD Principles are revised, when ecoDa issues new recommendations, when EU or Baltic governance expectations evolve, or when practical experience shows that additional guidance would be useful.

> Readers are therefore encouraged to treat this Handbook as an **evolving source of guidance** rather than a final and fixed publication. Its value will

depend not only on the text itself, but on how it is used in practice: in Board discussions, shareholder dialogue, management accountability, governance reviews and continuous improvement of companies across the Baltic region and beyond.

*When using this Handbook, readers should take into account that corporate governance **structures and legal terminology differ across Estonia, Latvia and Lithuania**. National company laws may refer to supervisory boards, councils, boards of directors, management boards or other collegial bodies, and the allocation of functions may differ depending on the jurisdiction and legal form of the company. To ensure clarity and consistency, this Handbook uses the term **"Board"** to mean the collegial governance body appointed by the shareholders, responsible for strategic direction, oversight and control of the company. Depending on the country and legal form, this body may be called a supervisory board, supervisory council, council or board of directors. Its key functions normally include appointing and, where necessary, replacing the head of executive management, approving strategy, setting goals and KPIs for management, overseeing performance, ensuring accountability, and monitoring major risks and results.*

*By contrast, the body or group responsible for day-to-day business execution is referred to in this Handbook as **"Management", "Management Team" or "Executives"**, even where national law may use the term "Management Board". Management is responsible for running the company's operations within the authority delegated by the Board and applicable law. The executive management team is usually headed by the CEO or, in jurisdictions where a separate CEO is not formally elected, by a designated member of the Management Board, i.e. Chairperson of the Management Board. Accordingly, unless the context requires otherwise, all references in this Handbook to the **CEO** should be understood as references to the person leading the executive management team, irrespective of the specific legal title or status assigned to that person under local law.*

DEFINITIONS AND ABBREVIATIONS

DEFINITIONS

The terms below are used throughout the Handbook in the meaning given here. Where the Estonian, Latvian and Lithuanian legal terms differ, the local terms are given in brackets.

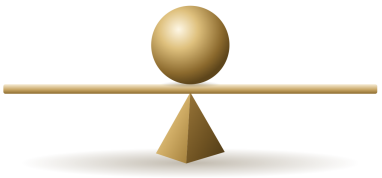
TERM	MEANING
Annual general meeting (AGM)	The ordinary meeting of shareholders held once a year to approve the annual accounts, decide on the distribution of profit, elect Board members and the auditor and decide other matters reserved to the shareholders by law or by the articles of association.
Balanced Board	A Board with the right mix of size, skills, experience, independence, diversity, continuity, renewal and dynamics to provide effective oversight, constructive challenge and sound decision-making.
Board	The collective body elected by the shareholders to set the direction of the company and to supervise its management. In this Handbook, “Board” refers to the Supervisory Board, also called the Council (Nõukogu in Estonia, Padome in Latvia, Stebėtojų taryba in Lithuania), in two-tier structures, and to the Board of directors (Valdyba in Lithuania) in one-tier structures.
Board charter	An internal document, approved by the Board or the shareholders, that sets out the Board’s role, composition, working procedures, committees, decision-making and reporting rules.
Board committee	A smaller group of selected Board members, established to prepare, monitor and advise on specific areas of the Board’s responsibility, such as audit, remuneration or nomination. Committees prepare decisions; the final decision remains with the Board.
Board competence matrix	A practical tool used to assess and plan the Board’s composition by mapping the skills, experience, knowledge and attributes needed for effective governance and long-term company success.
Board diversity	A Board composed of members with different backgrounds, experiences, skills, perspectives and personal characteristics, enabling broader insight, better challenge and more effective decision-making.
Board dynamics	The way Board members interact, debate, challenge, listen and make decisions together, shaping the quality of the Board’s collective judgement and effectiveness.
Board evaluation	The regular assessment of the performance of the Board as a whole, its committees, the Chair and the individual members, carried out as a self-assessment or with an external facilitator and leading to an improvement action plan.
Board member	A person elected or appointed to the Board; the term used in this Handbook in preference to “director”. Board members may be executive, non-executive or independent.
Board member rotation	Regular and orderly renewal of Board members over time, usually through term limits, staggered appointments, re-election cycles or maximum tenure rules.

TERM	MEANING
Board member succession planning	Planning how future Board members will be identified, selected and appointed to ensure that the Board continues to have the right mix of skills, independence, diversity and experience.
Board secretary	The person or function that supports the Board in its work: organising meetings, preparing agendas and materials, taking minutes, keeping corporate records, advising on governance procedures and compliance, and acting as the link between the Board, management and the shareholders. Also called company secretary or chief governance officer.
Business judgement rule	A legal principle under which Board members are not liable for business decisions that turn out badly, provided that the decision was taken in good faith, on an informed basis, within the Board's authority, without a conflict of interest and in the interests of the company.
Chair of the Board	The Board member elected to lead the Board: planning its work, chairing its meetings, ensuring effective discussion and decision-making, and maintaining the relationship with the CEO and the shareholders.
Chief executive officer (CEO)	The head of the executive team, responsible to the Board for the day-to-day management of the company and the implementation of its strategy.
Code of conduct (code of ethics)	A document approved by the Board that sets out the values, principles and standards of behaviour expected of Board members, managers and employees.
Comply or explain	The principle underlying corporate governance codes: a company either follows each recommendation of the code or explains publicly why it does not.
Conflict of interest	A situation in which the personal, financial or other interests of a Board member, a manager or a person related to them could influence, or appear to influence, the judgement they exercise on behalf of the company.
Control environment	The foundation of a company's governance and internal control system, reflecting its culture, values, accountability, roles, policies and behaviours that guide how decisions are made, risks are managed and rules are followed.
Corporate governance	The system by which companies are directed and controlled: the relationships between the management, the Board, the shareholders and other stakeholders, and the structure through which the company's objectives are set and the means of attaining them and of monitoring performance are determined.
Corporate governance code	A set of recommendations on good governance practice issued by a stock exchange or another body, applied by listed companies on a "comply or explain" basis and used as a benchmark by other companies.
Directors' and officers' liability insurance (D&O insurance)	Insurance that protects Board members and managers against claims for personal liability arising from the performance of their duties, and the company against the related costs.
Executive Board member	A top executive of the company who also serves on the Board (in one-tier structures).
Executive team (management)	The Management Board or the executive managers employed by the company and responsible for running its day-to-day business, reporting to the Board or directly to the shareholders (Juhatus in Estonia, Valde in Latvia, Vadovybė in Lithuania).

TERM	MEANING
General meeting of shareholders	The supreme body of the company, through which the shareholders exercise their rights; it meets annually (see AGM) and, where needed, at extraordinary meetings.
Independent Board member (INED)	A non-executive Board member who, in accordance with the applicable regulatory requirements and the company's internal policies, meets the independence criteria and has been assessed as independent by the Board (see sub-chapter 4.4).
Internal audit	An independent and objective assurance and advisory function that evaluates the effectiveness of governance, risk management and internal control, reporting functionally to the Board or its audit committee.
Key performance indicator (KPI)	A measurable indicator used to monitor the achievement of the company's or the CEO's objectives.
Management Board	In two-tier structures, the executive body responsible for managing the company, supervised by the Supervisory Board (Juhatus in Estonia, Valde in Latvia, Valdyba in Lithuania where it performs a management function).
Non-executive Board member	A Board member who is not employed by the company and is not engaged in its management or day-to-day operations.
One-tier and two-tier structures	In a one-tier structure a single Board, composed of executive and non-executive members, directs and supervises the company; in a two-tier structure a Supervisory Board (Council) supervises a separate Management Board (see sub-chapter 2.2).
Related party transaction (RPT)	A transfer of resources, services or obligations between the company and a related party (a shareholder, a Board member, a manager, a close family member or an entity controlled by them), regardless of whether a price is charged.
Risk appetite	The amount and type of risk that the company is willing to take in pursuit of its objectives, as set by the Board.
Shareholders' letter of expectations	A document in which the shareholders, typically the state or a controlling owner, set out their expectations of the company and its Board regarding strategy, performance, governance and reporting.
Stakeholders	Individuals and groups with an interest in, or influence over, the company's activities: shareholders, employees, customers, suppliers, creditors, regulators, local communities and others.
State-owned enterprise (SOE)	A company in which the state or a municipality holds a controlling interest.
Supervisory Board (Council)	In two-tier structures, the body elected by the shareholders to supervise the Management Board and to decide the matters reserved to it; also called the Council.
Three Lines Model	A model describing the roles in risk management and control: management (first line), risk, compliance and other support functions (second line) and internal audit (third line), with the Board providing oversight.
Tone at the top	The example set by the Board and senior management through their own conduct, decisions and communication, which shapes the culture of the company.
Whistleblowing	The reporting by employees or other persons of breaches of law, misconduct or unethical behaviour through a confidential channel, with protection against retaliation under the EU Whistleblowing Directive.

ABBREVIATIONS

ABBREVIATION	MEANING
AGM	Annual general meeting
AI	Artificial intelligence
BICG	Baltic Institute of Corporate Governance
CEO	Chief executive officer
CFO	Chief financial officer
CG	Corporate governance
COSO	Committee of Sponsoring Organizations of the Treadway Commission
CSDDD	Corporate Sustainability Due Diligence Directive
CSRD	Corporate Sustainability Reporting Directive
D&O	Directors' and officers' (liability insurance)
DORA	Digital Operational Resilience Act
ESG	Environmental, social and governance
ESRS	European Sustainability Reporting Standards
EU	European Union
GDPR	General Data Protection Regulation
IIA	The Institute of Internal Auditors
INED	Independent non-executive Board member
ISO	International Organization for Standardization
KPI	Key performance indicator
M&A	Mergers and acquisitions
NIS2	Directive on measures for a high common level of cybersecurity
OECD	Organisation for Economic Co-operation and Development
R&D	Research and development
RPT	Related party transaction
SOE	State-owned enterprise
SRD II	Shareholder Rights Directive II



CHAPTER

1

CORPORATE GOVERNANCE FRAMEWORK

What corporate governance is, which rules and documents make up a company's governance framework, and how to apply them in proportion to the company's size and ownership.

IN THIS CHAPTER

1.1	The concept of corporate governance	16
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1.1

THE CONCEPT OF CORPORATE GOVERNANCE

Corporate governance is "the system by which companies are ***directed and controlled***"[1], and the concept goes beyond formal legal requirements, setting a higher standard. The term corporate governance was coined in the mid-1970s together with ***agency theory,*** which prevailed in Anglo-Saxon countries and focused on large, centralised, hierarchical organisations that were then the key drivers of economic growth.

In 1984, ***stakeholder theory*** emerged, seeking to explain how value creation is possible in a world of great change and turbulence, to address the problem of the ethics of capitalism and to outline the managerial mindsets required. It is inherent in the continental corporate governance model through the composition of the Board (e.g. employee representation in Germany) and the consideration given to the interests of different stakeholders.

In 1991, ***stewardship theory*** was introduced, arguing that executive managers essentially want to be good stewards of the corporate assets and that their own reputation is tied to the firm's performance. Focus is placed on the overall design of the organisational structure so that managers can be empowered to take action. Stewardship codes are more principles-based than rules-based ("*comply or explain*") and should therefore provide more flexibility and enable Boards to maintain a long-term focus. Yet this approach does not incentivise innovation; moreover, legal reforms in different jurisdictions are so frequent that they create "compliance fatigue".

While limited liability joint-stock companies appeared in the mid-19th century, the world's first corporate governance code was developed by Sir Adrian Cadbury only in 1992, focusing on listed public companies. Before that, the role of directors was defined by company law or by financial and auditing standards. Recent developments indicate that all entities need good governance, and the ISO 37000:2021 Governance of Organisations Standard has been approved, guiding the governance of organisations of all industries, sizes, geographies, structures and objectives towards meeting their obligations so that their purpose is fulfilled.[2]

1 Cadbury Committee (1992), Report of the Committee on the Financial Aspects of Corporate Governance, London.
2 ISO 37000:2021, Governance of organizations – Guidance.

1.2
CORPORATE GOVERNANCE FRAMEWORK

A corporate governance framework serves as an important supporting structure: a set of rules and procedures that defines decision-making and accountability roles and the way in which the Board performs oversight of the company's operations. A well-established corporate governance framework promotes efficient operation of the company, accountability, fairness and openness in how the company operates and interacts with its stakeholders.

A good governance framework unifies decision-making, operational, risk management, reporting and financial processes to keep the Board informed and to help the Board make considered, data-based decisions that ensure the implementation of the company's strategy.

It is imperative that **governance documentation** is accurate and kept up to date. These documents establish the rules by which the company is governed, set out the rights and obligations of the shareholders, the Board and management, and provide evidence to shareholders and all other stakeholders of the governance processes and procedures in place.

Policies, codes, guidelines and other governance-related documents approved by the Board are important because they address relevant issues, such as the rules and principles for oversight of the company's operations, accountability, reporting and communications. They ensure compliance with laws and regulations, reflect the culture of the organisation, give guidance for decision-making and risk appetite, and streamline internal processes. These governance documents should be current and in line with legislation, regulations and good practice, as well as with the long-term goals and strategy of the company. They should not contain confidential information, because they should be made publicly available (for example, disclosed on the company's website) so that everyone understands the way the company is governed. An indicative list of the topics to be covered by corporate governance policies is provided in Annex 2.

A corporate governance framework should encompass:

1. Governance structure: the relationship between the shareholders, the Board (including its committees) and executive management
2. Roles and responsibilities of the shareholders, the Board, its committees and the CEO/Management Board
3. The appointment process for the Board and its committees

4. Performance of the Board and its committees (self-evaluation and performance improvement action plan), and review of the required Board competencies and composition
5. Remuneration of the members of the collegial bodies and the CEO/ Management Board
6. Ethics, “tone at the top” and company culture: how the company conducts itself and behaves
7. Strategy development, renewal and oversight of its implementation
8. Monitoring of the company’s performance (financial and non-financial)
9. Oversight of internal control, risk management, compliance, and internal and external audit
10. Relationship and engagement with shareholders and all other stakeholders
11. Disclosure and reporting (financial and non-financial, internal and external), transparency and accountability
12. Regular review and improvement of corporate governance practices within the company

To start building a corporate governance framework for a particular company, aim to answer these questions:

1. Who are the people with authority in your organisation, and what kind of authority do they need to have?
2. What information do those people need to access, and when?
3. What does the organisational structure look like?
4. How does the structure influence how decisions are made?
5. What are the organisation’s reporting obligations?
6. How does information need to flow inside and around the company?
7. What is the relationship between company units – and does this present any challenges in terms of accountability, authority or responsibility?
8. If there is a group of companies, how is the relationship between the group companies and the parent company established?
9. How is the relationship built with shareholders and all other stakeholders?

1.3
PROPORTIONALITY IN GOVERNANCE

Good corporate governance is not a "**one-size-fits-all**" model. While the core principles of governance are broadly the same for all companies — clear accountability, effective oversight, transparency, integrity, proper risk management and long-term value creation — the way these principles are applied should be proportionate to the company's size, ownership structure, complexity, public interest and risk profile. Proportionality does not mean weaker governance. It means applying governance practices in a practical, relevant and cost-effective way, so that governance strengthens the company rather than becoming a formal exercise.

For **listed companies**, governance expectations are usually the highest. They raise capital from public markets, have dispersed shareholders and are subject to market disclosure, investor scrutiny and regulatory requirements. Their Boards are expected to have a high level of independence, well-functioning committees, robust internal control and risk management systems, transparent remuneration practices, regular Board evaluation and high-quality disclosure. In listed companies, governance is not only a matter of internal effectiveness, but also a key condition for market trust, investor confidence and access to capital.

State-owned enterprises (SOEs) and municipally owned companies require governance that protects the company from political interference while ensuring proper accountability to the state, the municipality and the public. Their Boards must act in the best interests of the company, while recognising the company's public policy objectives where these are clearly defined by the owner. Proportionate governance in SOEs should include transparent selection and nomination of Board members, a clear letter of expectations from the owner, independent from political interference Boards, objective performance targets, transparent reporting, high-quality disclosure, and a clear distinction between the roles of the owner, the Board and management. In SOEs and municipally owned companies' governance is not only a matter of internal effectiveness, but also a safeguard against political influence which ensures the company's best interests and transparency.

Group companies create additional governance challenges because responsibilities are divided between the parent company and subsidiaries. The parent company may set group strategy, policies, risk appetite, reporting and accountability standards, but each subsidiary Board must still understand its own legal duties and act in the interests of the company it governs. Proportionate governance in groups should define reserved matters, delegation of authority,

reporting lines, intra-group transactions, risk oversight and the role of subsidiary Boards. Particular care is needed where subsidiaries operate in regulated sectors or different jurisdictions, have shareholders outside the group or are listed companies.

Private companies are not due to the same level of public disclosure as listed companies, but they still benefit significantly from sound governance. For growing private businesses, good governance helps professionalise decision-making, clarify the roles of owners, Boards and management, attract financing, manage risk and prepare for succession, sale, acquisition or listing of the company. In smaller companies, proportionality may mean a simpler Board structure, fewer formal committees and lighter reporting processes. However, the essential elements should remain: a clear strategy, competent and independent challenge, reliable financial information, proper controls and disciplined decision-making.

Family businesses require particular attention to the relationship between family, ownership, Board and management. Their strength often lies in long-term commitment, entrepreneurial culture and strong values. At the same time, they may face specific governance risks, including informal decision-making, unclear succession, conflicts between family members, or difficulties in separating family interests from company interests. Proportionate governance in family businesses should therefore include clear rules on family participation in the decision-making, succession planning, related-party transactions, dividend policy, employment of family members and the role of independent Board members. A family council, shareholders' agreement or family charter may be a good starting point in establishing good governance principles in the business.

In all types of companies, **proportionality should be based on substance rather than form**. The question is not whether the company has copied the governance structure of a large listed corporation, but whether its governance system is adequate for its purpose, risks and stakeholders. A smaller company may not need several Board committees, but it does need reliable financial controls. A family business may not need extensive public reporting, but it does need clear succession rules. An SOE may have public policy objectives, but it still requires commercial discipline and professional oversight. A group subsidiary may follow group policies, but its Board must still ensure its interest.

The **Board should regularly assess** whether the company's governance arrangements remain **proportionate and effective**. As companies grow, raise capital, internationalise, become more complex or acquire greater public significance, their governance should also evolve. Proportionality is therefore not a

justification for minimal governance; it is a disciplined approach to applying good governance in the right way, at the right level, and at the right stage of the company's development.

KEY TAKEAWAYS

A. Corporate governance is the system by which companies are directed and controlled. It goes beyond legal compliance and sets a higher standard of accountability, oversight and transparency.

B. The corporate governance framework is the set of rules and procedures that defines who decides what, who is accountable to whom, and how the Board oversees the company. It should be documented, kept up to date, aligned with legislation, good practice and the company's strategy, and made publicly available.

C. A complete framework covers twelve elements: from governance structure and roles, through Board appointment, performance and remuneration, ethics and culture, strategy, performance monitoring and oversight of control and risk, to stakeholder engagement, disclosure and regular review.

D. Building the framework starts with practical questions: who has authority, what information they need, how decisions are made, what must be reported, and how the company relates to its group, shareholders and other stakeholders.

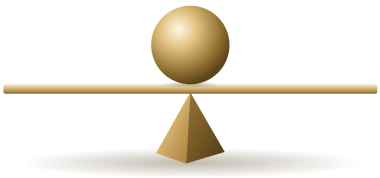
E. Good governance is not "one-size-fits-all". The core principles are the same for every company; their application should be proportional to the company's size, ownership structure, complexity, public interest and risk profile.

F. Proportionality is based on substance rather than form and never justifies minimal governance. Listed companies, SOEs, groups, private companies and family businesses each have specific priorities, but all need clear roles, reliable controls and independent challenge.

G. Governance must evolve with the company. The Board should regularly assess whether the governance arrangements remain proportionate and effective.

QUESTIONS FOR THE BOARD

1. *Do we have a clear, written and up-to-date corporate governance framework, and when did the Board last review it?*
2. *Are the roles and responsibilities of the shareholders, the Board, its committees and the CEO/Management Board clearly defined and understood, including which decisions are reserved for whom?*
3. *Are our governance documents (articles of association, Board charter, policies and codes) consistent with legislation, good practice and our strategy, and are they publicly available?*
4. *Does the Board receive the right information, at the right time, to exercise effective oversight and take considered decisions?*
5. *Which of the twelve elements of the governance framework are weakest in our company, and what is our plan to strengthen them?*
6. *Is our governance proportionate to our size, ownership structure, complexity, public interest and risk profile: neither copied from a large listed company nor reduced to a formality?*
7. *If we are a group company, an SOE or a family business, are the issues specific to us, such as reserved matters, the owner's expectations or succession, properly addressed?*
8. *As the company grows or changes, what would trigger a review of our governance arrangements?*



CHAPTER

2

CORPORATE GOVERNANCE IN THE BALTICS

How hard law and soft law shape governance in Estonia, Latvia and Lithuania, which Board models companies use, and how shareholders set out their expectations.

IN THIS CHAPTER

2.1	Hard law and soft law	24
2.2	Corporate governance models	25
2.3	Shareholders' letter of expectations	27

2.1
HARD LAW AND SOFT LAW

Legal acts entrench the most important and obligatory principles of corporate governance. The provisions of laws (hard law) typically establish minimum mandatory standards for the corporate governance system. Soft law is based on various instruments that are not legally binding (recommendations, guidelines, codes of conduct and similar) and provide higher, voluntarily applied standards for better corporate governance. The main aspects of hard law and soft law can be summarised as follows:

HARD LAW	SOFT LAW
– establishes minimum standards of conduct – legally binding – sanctions for violation of the law as the means of enforcement – form: laws, codes and regulations	– sets higher standards of conduct (best practice) through recommendations and guidelines – not legally binding, or with a binding force that is "weaker" than that of traditional law – based on the "comply or explain" principle – form: codes of conduct, guidelines and recommendations

Additional sources of soft law include various corporate governance principles, recommendations, guidelines and codes, such as the G20/OECD Principles of Corporate Governance, the OECD Guidelines on Corporate Governance of State-Owned Enterprises and national corporate governance codes.[3]

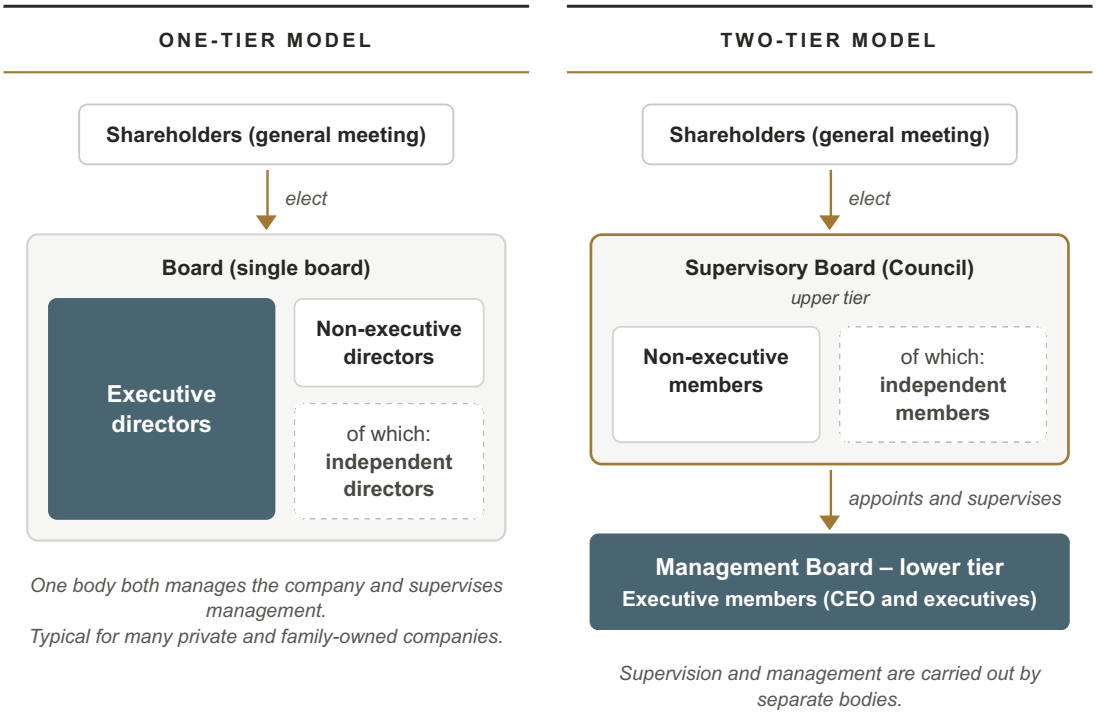
3 OECD (2023), G20/OECD Principles of Corporate Governance; OECD (2024), OECD Guidelines on Corporate Governance of State-Owned Enterprises.

2.2

CORPORATE GOVERNANCE MODELS

There is no single model of good corporate governance. Board structures and procedures vary both within and among countries. Some countries have two-tier Boards that separate the supervisory function and the management function into different bodies. Such systems typically have a Supervisory Board (in the Baltic states also called the Council) composed of non-executive members and a Management Board composed entirely of executives. Other countries have "unitary" (one-tier) Boards, which bring together executive and/or non-executive members.

Figure 2.1 **One-tier and two-tier corporate governance models**

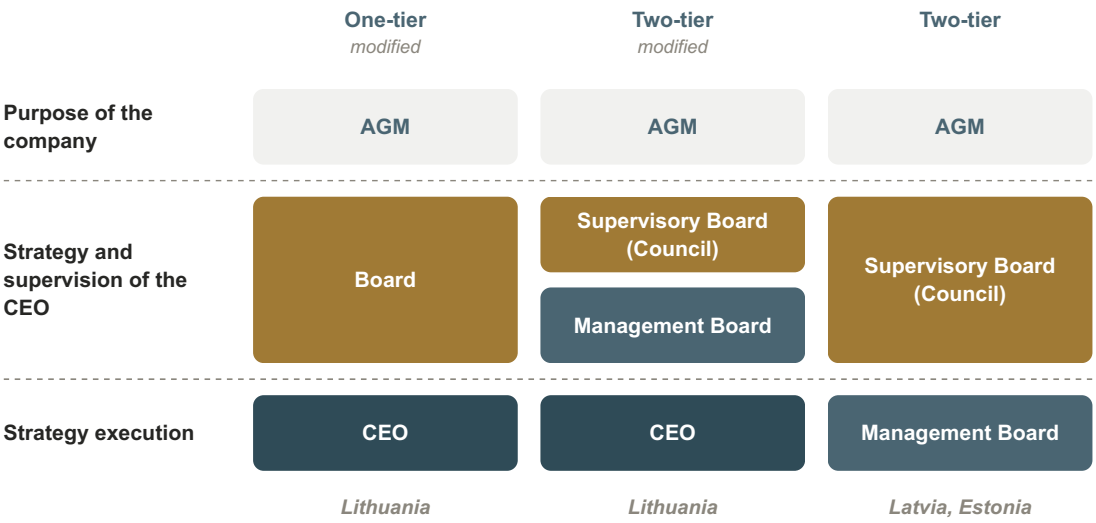


Some of the differences between the two models:

ONE-TIER	TWO-TIER
A single body responsible for both the management and the supervision of the company's operations	Clear distinction (including in liability) between the supervisory and management functions
Risk that non-executive directors align too closely with executive directors (less independence)	Supervisory Board members are more independent

ONE-TIER	TWO-TIER
Non-executive directors have more contact with the company itself	Supervisory Board members receive only limited information, and at a later stage (reduced involvement)
Faster decision-making. Lower administrative burden, as only one body needs to hold meetings and only one set of minutes has to be drawn up	Decision-making on specific matters may be delayed because Supervisory Board meetings are less frequent

Figure 2.2 Corporate governance models followed in the Baltic states



In the Modified structure CEO is a separate compulsory body. The particular features of the corporate governance models in each of the Baltic states:

ESTONIA	LATVIA	LITHUANIA
– **two-tier** – the Supervisory Board (*nõukogu*) and the Management Board (*juhatus*) – a private limited company is not obliged to have a Supervisory Board – a public limited company must always have a Supervisory Board	– **two-tier** – the Supervisory Board (*padome*) and the Management Board (*valde*) – the two-tier structure is mandatory for a joint-stock company	– **two-tier**: the Supervisory Board (*stebėtojų taryba*), the Management Board (*valdyba*) and the CEO* – **one-tier**: the Board (*valdyba*), composed of executive and/or non-executive members, and the CEO* – a private limited company is not obliged to have a Supervisory Board or a Management Board – a public limited company must always have a Supervisory Board or a Management Board *The *CEO is a separate, compulsory management body in both the two-tier and the one-tier model*

2.3

SHAREHOLDERS' LETTER OF EXPECTATIONS

Shareholders have specific expectations of what kind of business the company should be, what goals it should reach and how it should behave. These expectations can be written down in a document called the shareholders' letter of expectations. This letter is important because it helps the shareholders and the company's Board, which is responsible for achieving the shareholders' goals, to understand each other and work together effectively. The letter outlines the shared expectations and priorities of the shareholders and provides guidance to the Board in order to maximise long-term value and ensure that the company's activities benefit the shareholders, the communities and society as a whole. A shareholders' letter of expectations is usually more applicable to state-owned and municipally owned enterprises (SOEs and MOEs) and other companies with a relatively small number of shareholders, and less applicable to listed and other companies with very dispersed ownership. In the latter case, the definition of the purpose and long-term goals lies with the Board. In the case of SOEs and MOEs, the shareholders' letter of expectations, which should be publicly available on the company's website, plays an important role in protecting the Board and the company against political interference.

Several items are considered key in formulating the shareholders' letter of expectations:

- Shareholders' plans to hold the shares in the company
- Purpose, strategic destination and ultimate goal(s)
- Financial commitment and contingency planning
- Targeted returns (return on equity - ROE, required rate of return - RRR, dividends, value growth)
- Role of the company as a part of the economy and society

Through the shareholders' letter of expectations, the **shareholder(s) determine the direction of the company's development**. As the possible approaches can be mutually exclusive, one should be selected.

1. **Increasing long-term value.** Profits are invested in long-term value creation: R&D, patents, the development of unique ideas and the building of synergies. This also implies that shareholders are not concerned with fast returns or rapid

growth in market share; they are willing to invest in the development of a particular service or product without expecting a return in the short term.

2. **Maximising growth.** In taking this path, shareholders focus on future value rather than present value and prioritise future investment. Profits are used as a source of finance for growth, and an important financial objective is to increase turnover.
3. **Maximising profits**. In this case, shareholders target the withdrawal of dividends from the profits generated through increased efficiency and business development.

While setting out one of these three directions, the shareholders' letter of expectations should also include expectations regarding financial and non-financial objectives.

1. **Financial objectives** arise from the selected development direction and include expectations related to capital structure (leverage) and expected return.
2. **Non-financial objectives:**
    a. environmental responsibility – integrating environmental responsibility into company operations, adopting environmentally friendly practices, promoting energy efficiency and reducing carbon emissions;
    b. social responsibility – engaging in activities that benefit the community, such as supporting local initiatives, investing in community development programmes, promoting social inclusion and contributing to the overall well-being of residents;
    c. stakeholder engagement – actively engaging with residents, community organisations and other stakeholders to understand their needs, concerns and expectations;
    d. innovation and technological advancement **–** embracing innovation and using technology to enhance service delivery, operational efficiency and customer experience;
    e. corporate governance – upholding high standards of corporate governance, transparency and accountability, ensuring fair and ethical business practices and complying with legal and regulatory requirements;
    f. for public sector enterprises, other non-financial objectives (public policy objectives) may be defined; these should be financed by the state in a clear and transparent way.

The shareholders' letter of expectations should be defined for a period longer than the company's strategy and should be updated if there are significant changes in the shareholders' expectations, but not too often. It is bad practice for shareholders

to update their letter of expectations every year or every two years, because the Board would then have to adapt the company's strategy each time.

The Board is entitled to propose changes to the owners' expectations where there is an evident and very important need.

It is good practice for SOEs and MOEs to disclose the shareholders' letter of expectations and make it publicly available on the company's website and in its reports.

KEY TAKEAWAYS

A. Corporate governance in the Baltic states rests on both hard law and soft law. Laws set the minimum mandatory standards; codes, guidelines and recommendations set higher, voluntary standards, applied on a "comply or explain" basis.

B. The G20/OECD Principles of Corporate Governance, the OECD Guidelines on Corporate Governance of State-Owned Enterprises and the national corporate governance codes are the main soft-law reference points.

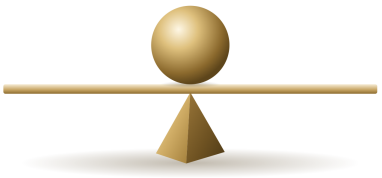
C. All three Baltic states use the two-tier model, with national differences; in Lithuania a one-tier option also exists, and the CEO is always a separate compulsory body.

D. A shareholders' letter of expectations sets out what the owners expect of the company: their plans for holding the shares, the company's purpose and strategic direction, financial commitments, targeted returns and the company's role in the economy and society.

E. The letter is most relevant to SOEs, MOEs and companies with a few shareholders. It should cover a period longer than the company's strategy, be updated only when expectations change significantly, and be publicly disclosed.

QUESTIONS FOR THE BOARD

1. *Which laws and which corporate governance code apply to our company?*
2. *Does our governance structure (one-tier or two-tier; Supervisory Board, Management Board, CEO) match what the law requires for our type of company, and does it work well in practice?*
3. *Are the roles, responsibilities and liabilities of the Supervisory Board, the Management Board and the CEO clearly separated and understood by all involved?*
4. *Do Supervisory Board members receive sufficient and timely information to exercise real oversight, and are they sufficiently independent of management?*
5. *Do we have a shareholders' letter of expectations, and does it state clearly the owners' chosen development direction and their financial and non-financial objectives?*
6. *Is the company's strategy aligned with the letter of expectations, and how do we handle differences between what the owners expect and what the Board considers achievable?*
7. *If we are an SOE or MOE, are public policy objectives clearly defined and separately financed, and is the letter of expectations publicly available on our website?*
8. *When was the letter of expectations last reviewed, and is there an agreed process for the Board to propose changes to the owners where circumstances require?*



CHAPTER

3

BOARD COMPOSITION, COMMITTEES, RENEWAL AND REMUNERATION

How to build a balanced and competent Board with effective committees, and how to renew, induct and fairly remunerate its members.

IN THIS CHAPTER

3.1	Balanced Board, its diversity and dynamics	33
3.2	Hard and soft competencies	35
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3.6	Remuneration of Board and committee members and chairs	44

The creation of the Board should be treated as a structured governance process rather than only a formal election of individuals. It should begin with a clear understanding of the company's ownership structure, strategy, scale, risk profile, regulatory environment and future development needs. Based on this assessment, shareholders should define the expected role of the Board, its mandate, composition, required competencies, independence expectations, diversity considerations, time commitment and working principles.

A Board competence matrix can be used to identify the knowledge, experience and behavioural qualities needed collectively by the Board, including sector expertise, finance, strategy, risk, legal, sustainability, digital transformation, people leadership and stakeholder understanding, among others.

The nomination and selection process should be transparent, objective and merit-based, with candidates assessed not only for their professional qualifications, but also for integrity, independence of judgement, ability to challenge constructively and willingness to act in the best interests of the company.

Once elected or appointed, Board members should receive a proper induction, including information on the company's business model, governance structure, strategy, risks, financial position, legal duties and key stakeholders. The first meetings of the newly created Board should focus on appointing the Chair, agreeing Board working procedures (developing and approving the Board Charter), confirming the annual calendar, establishing committees where appropriate, clarifying information flows with management and setting expectations for Board conduct and effectiveness.

3.1

BALANCED BOARD, ITS DIVERSITY AND DYNAMICS

A **Balanced Board** is crucial because it enables the Board to fulfil its core governance role effectively: providing strategic guidance, overseeing management, exercising independent judgement and safeguarding the long-term interests of the company. When the Board has the right combination of skills, experience, independence, diversity, size, continuity, renewal and constructive dynamics, it is better equipped to challenge assumptions, avoid groupthink, assess risks and opportunities from different perspectives, and make well-informed decisions. In this sense, Board balance is not only a formal composition issue; it is a key condition for Board effectiveness, responsible oversight and sustainable long-term value creation.

Balanced Board characteristics:

CHARACTERISTIC	WHAT IT MEANS
Board size	A Board should be large enough to provide the necessary skills, experience, independence, committee capacity and diversity of perspectives, but small enough to enable effective discussion, individual accountability and timely decision-making.
Independence and objectivity	A sufficient number of directors are able to exercise judgement free from undue influence by management, controlling shareholders or other interests. It is recommended to have a majority of independent directors on the Board.
Skills and expertise	The Board collectively has the knowledge needed for strategy, finance, risk, sustainability, digital transformation, people, regulation and the company's sector.
Experience and renewal	The Board should include both experienced members who understand the company well and new members who bring fresh ideas, while avoiding too much change or too little renewal.
Executive and non-executive roles	There is a clear balance between those responsible for management and those responsible for oversight, where applicable.
Constructive Board dynamics	The Board is able to debate openly, challenge respectfully, avoid groupthink and reach well-considered decisions.

There are two further characteristics of a Balanced Board that require particular attention.

Board diversity is an essential component of a Balanced Board. A Balanced Board is not achieved only by having diverse directors, but by ensuring the right combination of independence, skills, experience, continuity, renewal and diversity of perspectives needed for effective Board decision-making.

Board diversity explains *what kind of differences* the Board needs in order to avoid narrow thinking and improve decision-making. This may include:

- gender diversity;
- professional background;
- age and generational perspective;
- international experience;
- sector knowledge;
- functional expertise;
- stakeholder understanding;
- cognitive and behavioural diversity.

Board dynamics are an essential element of a Balanced Board, but they describe the quality of how the Board works, not only who is on the Board. A Board is not balanced only by its formal composition; it must also operate in a way that enables constructive challenge, open discussion, mutual respect, effective use of different perspectives and collective decision-making.

3.2
HARD AND SOFT COMPETENCIES

A Board with the **right and complete mix of competencies, skills and knowledge** is more effective in governing and guiding a company. Not every Board member needs to have all of them, but the Board as a whole should have a balanced mix of these competencies. This leads to better decision-making, risk management, strategic planning and overall performance. The Board's composition should align with the company's needs, challenges and strategic goals at a given period, and it should be reviewed during the annual (self-)assessment. If any changes are needed, the Board should take appropriate measures to address them (develop or improve skills, or suggest to the shareholders the replacement of a particular Board member or the enlargement of the Board).

In addition to hard competencies, an effective Board also needs strong **soft competencies** and behavioural qualities. These are essential because Board effectiveness depends not only on what directors know, but also on how they work together and how each of them behaves.

The objective is not for every Board member to be an expert in every area, but for the Board as a whole to have the collective capability, diversity of perspectives and behavioural quality needed to provide effective oversight, challenge management and support sustainable long-term value creation. It is advisable that **at least two Board members have sufficient understanding of the same key hard competence**, especially where that competence is critical for the company. This does not necessarily mean two full experts, but the Board should avoid a situation where only one person is able to understand, challenge or explain an important area. Such an arrangement avoids overdependence on one individual, improves the quality of challenge, supports the continuity of Board work (if one member leaves) and supports Board committee work, where several members should be able to contribute meaningfully.

An indicative list of hard and soft competencies is provided in Annex 1.

3.3
BOARD COMPETENCE MATRIX

A Board competence matrix is a tool that assists a company, its Board and shareholders in assessing and planning the composition of the Board, to ensure that it has the correct combination of skills, experience and knowledge to govern and steer the company efficiently and successfully. The main benefits of a Board competence matrix include:

- Strategic alignment. Ensuring that Board members have the right set of skills and knowledge helps them to understand and contribute to the strategic direction of the company, in better alignment with the company's strategic objectives.
- Increased confidence among shareholders and investors. A well-balanced and professional Board may boost shareholder trust.
- More competent decision-making. With the right set of competencies, the Board can make informed decisions more efficiently, which directly contributes to more professional and faster Board work and more effective governance, both crucial for the company's success.
- Improved risk management. A varied set of skills on the Board can help with risk management. Board members with financial, legal, industry-specific and other knowledge can help to identify and manage risks.
- Enhanced innovation, adaptability and resilience. A Board with diverse competencies can bring fresh perspectives and innovative ideas. Board members with various backgrounds and experience are more likely to challenge the status quo and help the company adapt to changing market conditions and withstand uncertainties and disruptions.

Table 3.1 **Example of a Board competence matrix (illustrative)**

		BOARD MEMBERS				
NO.	COMPETENCY / EXPERTISE	#1	#2	#3	#4	#5
1	Financial management, accounting	X				
2	Industry expertise, including knowledge of the sector		X	X		
3	Leadership	X				
4	Global experience					
5	International business development	X				

		BOARD MEMBERS				
NO.	**COMPETENCY / EXPERTISE**	**#1**	**#2**	**#3**	**#4**	**#5**
6	CEO or senior management experience					
7	Strategy development	**X**	**X**	**X**		
8	Strategic thinking, analysis of information					
9	Corporate governance					
10	Compliance					
11	IT and technological expertise	**X**	**X**			
12	Marketing experience	**X**				
13	Risk governance, experience in developing and implementing risk management systems	**X**		**X**		
14	Legal expertise			**X**		
15	HR management		**X**			
16	Change management	**X**	**X**	**X**		
17	Experience on other Boards	**X**				
18	Public relations, communications					
...	...	...	...	...	...	...

It is good practice to define the key competencies and the additional competencies required on the Board.

Ideally, more than one Board member should possess a specific skill or competence, so that they can challenge and ask questions.

The Board competence matrix is part of the succession planning and Board assessment processes, and responsibility for these processes lies with the Board and its nomination committee (where such a committee exists).

It is good practice to review and update (if needed) the Board competence matrix, including the full list of competencies, at each annual Board performance assessment.

3.4
BOARD COMMITTEES

Purpose of the Board committees

Boards should consider setting up specialised committees to support the full Board in performing its functions, particularly in respect of audit and, depending on the company's size and risk profile, also in respect of risk management, nomination and remuneration. Where justified by the size of the company and its Board, the use of committees may improve the work of the Board.

In addition to enhancing the Board's effectiveness, committees usually allow for a division of labour and a more efficient allocation of tasks among members. They also help to make better use of members' time and expertise, which contributes to specialisation of knowledge and more precise advice to the Board.

Board committees may be tasked with considering emerging trends, including ESG, diversity, increased stakeholder activism, and risks and opportunities related to evolving digital technologies (e.g. artificial intelligence). It is important that stakeholders receive a full and clear picture of the committees' purpose, duties, composition and activities (e.g. on the corporate website).

Establishment of committees

Three types of Board committee – audit, nomination and remuneration – are most commonly required by law or listing rules, or recommended by corporate governance codes, in most jurisdictions. The Board may establish other committees, such as a risk committee, strategy committee, sustainability committee, innovation committee, social and ethics committee, policy committee, finance committee, negotiations committee or facilities committee. A Board committee may have two or more roles. The Board may also form a task force to deal with a specific, time-bound issue.

When Board committees are established, their mandate, clear accountability rules, access to information, budget and external advice, composition and working procedures should be well defined by the Board (e.g. in a committee charter). While committee charters differ across committees and companies, they have some common features. They usually comprise the following elements:

- mission statement;
- role, purpose and responsibilities;
- delegation of authority, extent of power and decision-making abilities;
- composition and structure;

- membership requirements and procedure for meeting attendance by non-committee members;
- frequency of meetings;
- terms of access to internal and external resources and information;
- accountability requirements to the Board and formalities;
- special duties and powers of the committee chair, and tenure.

The authority of each committee should be determined by the Board itself. Committees should perform their duties according to the authority delegated to them. The composition of committees influences their effectiveness and performance. Members of each committee should be selected on the basis of their competencies.

It is suggested that all Board committees should comprise Board **members only** (i.e. no external persons) and should have a majority of independent Board members. If a Board committee needs specific expertise, it can engage outside experts; where this expertise is needed permanently, however, the person should become a member of the Board and then be delegated to that committee. Committees should be chaired by independent Board members.

Committee size usually depends on the needs of the Board and the way it is organised, the size of the company, and an assessment of the number of members needed to carry out the specific work. There is no optimal number of members, though committees are expected to remain efficient, not overburdened and not too costly. Most jurisdictions require or recommend that at least the audit, nomination and remuneration committees have three members and that all or a majority of them are independent.

For information on the working methods of Board committees, see sub-chapter 6.4.

3.5

BOARD RENEWAL – SUCCESSION PLANNING, ROTATION AND INDUCTION

The Board has a duty to ensure that its composition, competencies, knowledge, experience, diversity and dynamics fit the needs of the Board and the company over the long term, in order to maximise value for the shareholders and all relevant stakeholders. Board members who serve for too long often become too comfortable in their position, establish too close a relationship with top management, do not exercise effective control and do not challenge management enough, and thus contribute less to long-term value creation.

One of the main questions to ask about the performance of each Board member is whether they **deliver enough value** to the work and performance of the Board and to the company.

It is very important for the Board to ensure **continuity** and institutional knowledge. Long-tenured directors have experience of, and insight into, the company's strategy, operations and culture that can prove indispensable. It is not good practice to replace most of the Board members where there are no special reasons (such as underperformance or negligence), and it is recommended to retain at least some members.

Board member succession planning

Board succession means planning how future Board members will be identified, selected and appointed to ensure that the Board continues to have the right mix of skills, independence, diversity and experience.

Board member succession is the planned and structured process of identifying, preparing and appointing new Board members when existing members complete their term, resign, retire or when the company's strategic needs change. It is an important element of Board effectiveness because the Board must remain capable of providing proper oversight, constructive challenge and strategic guidance over time.

Board member succession is needed to ensure continuity, renewal and the right mix of competencies. Without proper succession planning, the company may face sudden gaps in expertise, loss of institutional memory, weak committee composition or overdependence on individual directors. A well-planned succession process helps the Board remain balanced, independent and fit for purpose as the company

evolves, its risks change and new regulatory, technological, sustainability or market challenges emerge.

The benefits of Board succession planning are significant. It supports a more stable and predictable renewal of the Board, reduces the risk of rushed or politically driven appointments, strengthens diversity and independence, and helps align Board composition with the company's long-term strategy. It also improves shareholders', investors' and stakeholders' confidence, as it shows that the company treats Board composition as a strategic governance matter.

To carry out Board succession properly, the Board should regularly assess its current and future composition needs. This can be done through a Board competence matrix, Board evaluation, review of committee needs, analysis of upcoming term expiries and discussion of the company's future strategic priorities. The nomination committee (where established) should lead this process and prepare clear criteria for new Board members, including required skills, experience, independence, diversity and behavioural qualities. Succession should be planned early, transparent in process, based on merit and aligned with the company's governance framework. The objective is not only to replace departing directors, but to continuously ensure that the Board has the right people, capabilities and dynamics to support sustainable long-term value creation.

Board member rotation

Board rotation means the regular and orderly renewal of Board members over time, usually through term limits, staggered appointments, re-election cycles or maximum tenure rules. Rotation helps avoid stagnation, excessive entrenchment and overdependence on long-serving individuals.

There are several steps that the Board should take on a regular basis to ensure that its composition fits the needs of the company and that there is a smooth plan for Board member rotation:

1. Review the company strategy at least annually and (re)identify the key strategic objectives.
2. Based on the key strategic objectives and the current and expected business environment, define what competencies are needed on the Board to govern and oversee the company efficiently. Individual traits should not be discounted either. It is highly recommended to use the Board competence matrix for this purpose.
3. Perform an annual self-assessment (see sub-chapter 6.6) of the Board as a whole, of each Board member and of the Chair of the Board, to identify what backgrounds, competencies and skills are present and what is missing, and

what the performance and contribution of each member and of the whole Board are. The self-assessment will give insights into what should be changed on the Board, what new backgrounds, competencies and skills are needed and what knowledge should be acquired.

As a result, the Board should define how these gaps will be covered. If any member needs to be replaced, the shareholders should be informed and the search for a new candidate should start, involving the nomination committee and (recommended) an executive search company.

4. Since any change in the Board's composition can be made only by the shareholders, the planning of the replacement process should take into account the timing of shareholders' meetings.

It is important to note that any Board member may be replaced regardless of their tenure if the Board and/or the shareholders see the need for it. A Board member who is to be replaced should place the interests of the company above their own; otherwise, they risk damaging their reputation.

If the Board finds that, with its current number of members, it cannot ensure efficient and professional Board work, it must propose to the shareholders (with supporting arguments) that the Board be enlarged. For example, the company may be acquiring another entity, undergoing a major transformation or planning a significant expansion into other markets, and may need all its current competencies plus an additional set of competencies and experience. A similar reason may arise when the Board decides to establish Board committee(s) and finds that there are not enough members with the desired competencies. Since members of Board committees must be Board members only, the Board should propose to the shareholders that the number of Board members be increased.

The process of Board renewal should be defined in a Board renewal policy or a similar document approved by the shareholders, and should be publicly available. This allows for better engagement with shareholders and all other stakeholders.

All changes in the Board's composition (including the reasoning) should be communicated by the company to all stakeholders.

Induction of the newly appointed Board members

Newly appointed Board members should receive a structured induction organised under a Board-approved induction policy and/or procedure. It should define the purpose, scope, timing, content, responsibilities and documents to be provided to each new Board member. The Chair should be responsible for ensuring that the induction is properly planned and aligned with the Board's expectations, while the

corporate secretary should coordinate the practical process, prepare the induction pack, arrange meetings and maintain records. The CEO and senior management should provide briefings on the company's strategy, business model, financial position, operations, key risks, internal controls, regulatory environment and main stakeholders. The induction should also cover the company's governance framework, Board and committee working practices, annual calendar, reporting lines, decision-making procedures, information flows and expectations regarding preparation, attendance, confidentiality, conflicts of interest and collective responsibility. It should include meetings with the Chair, CEO, key executives and, where relevant, major shareholders, as well as access to core corporate documents. A well-organised induction helps new Board members understand the company quickly, contribute effectively from the beginning and exercise independent judgement in the best interests of the company.

3.6

REMUNERATION OF BOARD AND COMMITTEE MEMBERS AND CHAIRS

Shareholders should establish a clear and transparent remuneration policy for Board members, based on a proposal made by the Board. This policy should set out the principles, components and procedures for determining Board member remuneration.

As defining Board remuneration is a critical aspect of corporate governance, it should be done taking into account several key factors that help to ensure transparency, fairness, alignment with the company's objectives and compliance with regulatory requirements. The main considerations are:

Company size and complexity. The size, industry and complexity of the company should be a fundamental consideration. Larger and more complex organisations usually require more time and expertise from their Board members. A group of companies is usually more complex than a single company.

Industry practices. Benchmarking against peer companies within the same industry or sector is a common practice. Understanding what other companies of similar size and complexity pay their Board members can help to ensure that remuneration is adequate.

Market conditions. Economic conditions, market trends and the competitive landscape can influence Board member remuneration. A company may need to adjust Board members' remuneration to attract and retain top talent in a highly competitive market.

Risk and liability. It is recommended to consider the level of risk and potential liability associated with the role of a Board member, especially in industries with higher regulatory scrutiny or complex legal environments.

Legal, regulatory and ethical considerations. Shareholders should ensure that Board members' remuneration is not only legally compliant but also ethically defensible. Unjustified, excessive or unduly low remuneration could draw negative attention or criticism.

Board roles and responsibilities. All Board members should be remunerated equally for the performance of their duties as Board members. Members of Board

committees should receive additional remuneration for committee work, equal for all members of the same committee. The Chair of the Board and the chairs of Board committees receive higher remuneration because of their additional duties.

General practice in defining the level of Board member remuneration is to use the total remuneration (fixed and variable) of the CEO as a benchmark. Depending on the time commitment, this could be in the range of 10–20 per cent of the CEO's total remuneration. For instance, if the Board holds 4–6 meetings rather than 10–12 meetings per year, remuneration should be aligned accordingly.

It is good practice to define fixed (monthly or quarterly) remuneration, because a Board member is involved in the company's matters not only during Board meetings but also between meetings. It is not good practice to set performance-based remuneration for Board members, because it could increase risk-taking among Board members and create potential risks for the company. This is even more relevant in the case of the Chair of the Board or the chairs of Board committees.

Members of Board committees should also receive additional remuneration, but at a lower level than Board member remuneration, taking into consideration that committees do not take decisions and do not bear legal responsibility. The level of time commitment should also be considered. If a committee works the same or a similar amount of time as the Board, the additional remuneration of a committee member should be in the range of 50–70 per cent of a Board member's remuneration. If the time commitment is lower, the remuneration should be lower too.

Because of their higher engagement, the remuneration of the Chair of the Board should be 2–3 times higher than the remuneration of Board members. Similar guidance applies to the chairs of committees, with a lower multiplier (i.e. 1.5–2.0 times the remuneration of a member of the respective committee).

A company should also reimburse all travel, accommodation and other expenses of Board members related to the performance of their duties. In addition, the company should pay for (and budget for) the development of Board member competencies, in order to keep them up to date on industry trends and related topics.

It is good practice to disclose all elements of Board members' remuneration in annual reports and other relevant documents. This is usually mandatory for listed and state-controlled companies. Transparency builds trust among shareholders and the broader stakeholder community.

It is important for companies to continually review and update their remuneration practices to remain competitive and aligned with evolving governance standards and market conditions.

Defining board member remuneration is a complex process that requires careful consideration of all of these aspects, balancing the need to attract and retain top talent with the responsibility to protect the interests of the company, its shareholders and stakeholders.

KEY TAKEAWAYS

A. Creating a Board is a structured governance process, not merely a formal election. It starts from the company's ownership, strategy, scale and risk profile, and from a clear definition by the shareholders of the Board's role, mandate, composition, required competencies and independence expectations.

B. A Balanced Board combines the right size, independence, skills, experience, a clear division between executive and non-executive roles, and constructive dynamics. Diversity of perspectives and the way the Board works together matter as much as who serves on it.

C. The Board as a whole, not each member, must hold the necessary hard and soft competencies. At least two members should understand each key competence, so that no important area depends on one person.

D. A Board competence matrix is the practical tool for assessing and planning Board composition. It supports strategic alignment, better decision-making and risk management, and should be reviewed at each annual Board assessment.

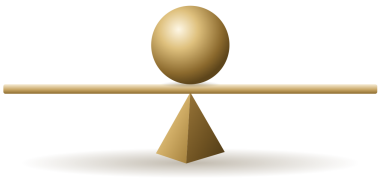
E. Board committees (audit, nomination, remuneration, strategy, etc.) improve Board work through specialisation. They should consist of Board members only, have a majority of independent members, be chaired by an independent member and operate under a clear charter. Committees do not make decisions, Board does.

F. Board renewal requires planned succession, orderly rotation and structured induction. Overly long tenure erodes independence, while replacing most members at once destroys continuity; the balance is managed through annual review of strategy, competencies and performance, and a publicly available Board renewal policy.

G. Board remuneration should be set by the shareholders under a clear policy: fixed rather than performance-based; equal for all members, with additional remuneration for committee work; higher for the Chair and committee chairs; benchmarked against the CEO's total remuneration; and fully disclosed.

QUESTIONS FOR THE BOARD

1. *Have the shareholders clearly defined the Board's role, mandate, required competencies and independence expectations, and does our current composition match them?*
2. *Is our Board balanced in size, independence, skills, experience and diversity, and does it work through open debate and constructive challenge rather than groupthink?*
3. *Do we maintain a Board competence matrix, and when was it last reviewed against the company's strategy and the results of the Board assessment?*
4. *Is any critical competence held by only one Board member, and what is our plan to address that dependence?*
5. *Do our committees have clear charters, an appropriate size, a majority of independent members and independent chairs, and do stakeholders have a clear picture of their work?*
6. *Do we have a succession plan and a rotation approach that ensure renewal without losing continuity, and is our Board renewal policy publicly available?*
7. *Do newly appointed members receive a structured induction under an approved policy, with the Chair accountable for it and the corporate secretary coordinating it?*
8. *Is our remuneration policy for Board and committee members and chairs clear, fixed rather than performance-based, benchmarked, ethically defensible and fully disclosed?*



CHAPTER

4

DUTIES AND RESPONSIBILITIES OF THE BOARD, THE CHAIR AND MEMBERS

What the law and good practice expect of the Board as a whole, of its Chair and of each Board member, including independent members.

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4.1
BOARD

The Board implements corporate governance by providing strategic leadership and oversight. Its key purpose is to ensure the sustainable success of the company while meeting the interests of all shareholders and balancing the interests of stakeholders.

All the duties apply to each member of the Board individually and to the whole Board *in corpore*. The Baltic legal systems emphasise the Board's duty towards the company's best interests, while shareholders' and stakeholders' interests are derived from it.

This duty is defined as a fiduciary duty, and typically requires more than the law defines. It implies making decisions with care and diligence, in good faith, always with the goal of protecting the company's best interests and avoiding conflicts of interest. It is always a balancing act, as the exercise of oversight duties must leave management the freedom to execute the strategy without undue interference.

There are two main types of fiduciary duty:

1. ***Duty of Care***
    i. the responsibility always to act within the law and the authority granted by the shareholders and defined in the Articles of Association, and to make informed decisions in order to exercise sound judgement with the highest degree of professional skill, caution and critical awareness of risk. This implies taking responsibility for collecting necessary and sufficient information, examining assumptions and considering alternative options, including obtaining expert advice where appropriate.
    ii. Board members are required to perform their duties with such due diligence as would be applied by a prudent executive in the same circumstances:

a. not just a prudent person, but a prudent executive (a higher standard: an average, reasonably experienced business leader, while the subjective circumstances, such as the experience and knowledge of the particular person, would also be taken into account by the courts);

b. comparable circumstances (including available resources and the economic state of the particular company).

2. ***Duty of Loyalty*** requires a member to put the best interests of the company first at all times, to disclose upfront any and all relevant information that could affect their ability to carry out their duties for the benefit of the company, to

maintain the confidentiality of all information relating to the company, whether written or spoken, and never to use it for personal gain, and to abstain from other conflict-of-interest situations.

Board responsibilities include, among other relevant items and subject to the country-specific legal framework:

1. Determine the company's purpose, vision, mission and values
2. Guide strategy development, approve the strategy and oversee its implementation
3. Ensure that the company has sufficient resources and tools, including a proper organisational structure, to implement the strategy
4. Focus on long-term sustainable value creation beyond financial returns
5. Develop, improve and monitor the corporate governance framework
6. Challenge assumptions, set ambitious goals and support management in achieving them
7. Approve the medium-term business plan, budget and investment plans, and oversee their implementation as well as financial and non-financial performance
8. Oversee management (including appointing and dismissing the CEO and/or Management Board, defining remuneration and incentive schemes, and ensuring succession planning and talent development)
9. Ensure that the control environment, risk management, compliance, and external and internal audit are effective
10. Report to shareholders and other stakeholders, and oversee disclosure and internal and external communications
11. Establish a framework to safeguard the reputation of the company and ensure the transparency and ethical behaviour of the company
12. Oversee stakeholder relationships and ensure that the interests of stakeholders are taken into account
13. Establish Board committees where needed and ensure their efficient work and contribution to the Board's activities
14. Take an active leadership role in shaping the company's direction, advising management and stepping in when necessary to ensure the organisation's long-term success and sustainability
15. Assess the Board's own performance and develop continuous improvement plans

To implement the above Board functions efficiently, each Board member shall:

1. participate in person in the meetings of the Board and vote on all agenda items, except in the cases established by law where the Board member does not have the right to vote;
2. familiarise themselves with the agenda items, draft resolutions and other documents associated with the meetings of the Board;
3. actively participate in the discussion of the agenda items;
4. constantly deepen their knowledge and develop the qualifications necessary for the proper performance of the functions of a Board member, in order to fully understand the company's business, its environment and trends, and to perform tasks efficiently and take professional decisions;
5. perform other obligations established by law, the Articles of Association and the Board regulations or charter.

4.2
CHAIR OF THE BOARD

The Chair acts as an important link between the Board and the organisation's management via the CEO, and is responsible for the leadership of the Board, but is not the "boss" of the Board members. The Chair is appointed to the position by the Board members, rather than directly by the shareholders or the major shareholder(s). The Chair's impact on the overall success of the Board's work should not be underestimated, because the Chair of the Board sets the tone at the top of the organisation, which cascades down and affects the whole company, its performance and its long-term success.

There is an option to appoint a Vice-Chair of the Board, whose main responsibility is to take on the Chair's role when the Chair is absent or unavailable, e.g. to run Board meetings or represent the company when the Chair cannot attend.

The Chair is responsible for the leadership of the Board, including:

1. facilitating a proper flow of information to the Board;
2. facilitating the effective functioning of the Board, including managing the conduct, frequency and length of Board meetings;
3. communicating the views of the Board, in conjunction with the CEO, to the organisation's shareholders, broader stakeholders and the public.

In performing this role, the Chair's responsibilities also include:

1. in consultation with the CEO and/or company secretary:
    a. setting the agenda for the matters to be considered by the Board;
    b. ensuring that the information provided to the Board is relevant, accurate, timely and sufficient to keep the Board appropriately informed of the performance of the organisation and of any developments that may have a material impact on the organisation or its performance;
    c. ensuring that communications with stakeholders are accurate and effective;
2. ensuring that the Board as a whole has the opportunity to maintain an adequate understanding of the organisation's financial position, performance, operations and affairs generally, and of the opportunities and challenges facing the organisation;
3. facilitating open and constructive communication among Board members and encouraging their contribution to Board deliberations;

4. overseeing and facilitating Board, committee and Board member evaluation reviews and succession planning;
5. liaising with the CEO as the primary contact between the Board and management; and
6. liaising with and counselling, as appropriate, Board members.

4.3
BOARD MEMBERS

In one-tier Boards there may be both executive and non-executive directors, while the Supervisory Boards of the two-tier structure consist of non-executive directors only. It is recommended that Boards have as many non-executive directors as possible and, among them, the maximum number of independent directors. Executive directors cannot perform one of the most valuable responsibilities of the Board: challenging management when goals and key performance indicators (KPIs) are set. For instance, if management makes a proposal to the Board to decide on the launch of a certain investment project, executive Board members will not involve themselves in challenging the assumptions of the proposal or the ambition of the proposed targets and goals, because these proposals were made by themselves.

Another reason to have more non-executive directors is the opportunity to bring additional competencies to the Board and the company.

Executive and non-executive directors have the same duties and responsibilities on the Board.

4.4
INDEPENDENT BOARD MEMBERS

Benefits of independent Board members

Although each Board member must act with independence of mind (i.e. should be able to make their own reasoned, objective and independent decisions in performing their Board member functions), good governance requires that the majority of Board members should also be formally independent.

The benefits of having independent members on the Board include:

- Availability of additional competencies, skills, experience and knowledge;
- Unbiased and objective judgement of the company and its prospects;
- Strong ability to challenge the status quo and to identify weaknesses, strengths and opportunities;
- Improved credibility of the Board and the company;
- Increased stakeholder trust;
- Assistance in resolving conflicts that may arise among Board members;
- Reducing or even preventing groupthink[4] on the Board;
- Improved overall proficiency of the Board and the value it creates;
- Overall improvement of corporate governance practices and organisational culture.

Independence principle and criteria

Formal independence means that the Board member does not have any current or recent material relationship or links with the company, its affiliates, their management or the significant direct or indirect shareholders of the company or its affiliates, and does not participate in the day-to-day operations of the company. This **principle** of the absence of material relationships or links serves as the **main measure for evaluating the formal independence** of a Board member.

In practice, to aid the assessment of the formal independence of Board members and to clarify which situations may affect it, ***criteria are established*** that usually indicate whether or not a member is formally independent. These criteria are used as presumptions that may be rebutted by reasoned and evidence-based arguments

4 *Groupthink* is a phenomenon that occurs when a group of individuals reaches a consensus without critical reasoning or evaluation of the consequences or alternatives. Groupthink is based on a common desire not to upset the balance of a group of people. This desire creates a dynamic within a group whereby creativity and individuality tend to be stifled in order to avoid conflict.

as to why the member, despite meeting specific criteria, may nonetheless be deemed formally independent.

Sample lists of formal independence criteria may be provided in:

- Company laws applicable to the company (which may be mandatory for some companies, e.g. listed companies, and serve as a minimum requirement);
- Other laws or regulations (e.g. special requirements for companies operating in specific regulated sectors, such as financial institutions);
- Guidelines, corporate governance codes and principles, best practices and other soft law (e.g. this Handbook, the corporate governance code of the stock exchange on which the company's shares are listed, and the other examples provided at the end of this section).

The company should decide and record which criteria it will apply to assess and establish the formal independence of its Board members. When selecting the criteria, the company should take into account the mandatory legal and regulatory requirements, the principles set out in soft law (guidelines and codes), and its individual circumstances, which may affect the selection and description of the criteria (e.g. listed entities should take into account the corporate governance code of the market on which their securities are listed; the shareholding threshold for a "material shareholding" will probably be significantly lower for listed companies and/or companies with an otherwise diverse shareholder base; and the company's overall turnover, the turnover it generates from its top clients or the value of its top supply contracts may affect how the company defines a "material" business relationship).

Based on the Baltic company laws and the soft-law recommendations listed at the end of this section, BICG proposes the criteria below as guidance for establishing the independence of a Board member. A Board member may be considered independent if they:

1. are not, and have not been for at least the past two (2) years, employed by the company or its affiliates;
2. do not have a material relationship with the significant direct and/or indirect shareholder(s) of the company or its affiliates. The threshold of shareholding that qualifies as "significant" may vary depending on the company (e.g. mandatory thresholds may be established for regulated entities, and share listing or widely dispersed shareholdings may merit lower thresholds) and should therefore be defined by the company itself, taking into account the applicable regulatory requirements;

3. do not have, and have not had for at least the past two (2) years, a material business relationship or any other material interest with the company or its affiliates (either directly or indirectly through a related party). The definition of materiality may vary depending on the circumstances of the company and should therefore be defined by the company itself, taking into account the applicable regulatory requirements;
4. do not receive, and have not received for at least the past two (2) years, any additional remuneration from the company or its affiliates other than the fees for the performance of Board member functions;
5. are not employed as an executive officer of another company on whose Board any of the company's executives serve;
6. are not, and have not been at any time during at least the past three (3) years, affiliated with or employed by a present or former auditor of the company or any of its affiliates;
7. are not (i) a close relative, partner or spouse of any individual who would not meet any of the criteria set out in points 1 to 6, or (ii) a close relative, partner or spouse of a member of the Board of the same company or any of its affiliates;
8. have not served on the Board of the company as an independent director for more than 8–10 years;
9. do not have any other interest or relationship (formal or personal) that could interfere with their ability to act in the best interests of the company;
10. are financially independent from the shareholders (i.e. a substantial part of the Board member's income is not received from companies of the same shareholder(s)).

The above list is non-exhaustive and further criteria may be added to address the individual circumstances of the company.

Board members' formal independence criteria and the evaluation process are usually described in the company's Board member independence policy or another policy. In major companies with well-established Boards and/or a diverse shareholder base, such a policy is approved by the Board itself. In companies establishing the Board as a new corporate body and appointing the Board for the first time, or in smaller companies with a small number of non-executive Board members and/or only a few shareholders, the Board member independence policy may be approved by the general meeting of shareholders.

Recommended proportion of independent members, independence assessment and transparency

Ideally, all Board members should be independent. If this is not possible, good practice requires that the majority of Board members are formally independent.

The formal independence of each Board member should be evaluated:

1. prior to their nomination;
2. upon their appointment; and
3. regularly thereafter (e.g. annually) or *ad hoc* (upon a change or the occurrence of new circumstances that could affect the member's formal independence).

A company should be transparent about the formal independence of its Board members and should disclose:

- the criteria on the basis of which the formal independence of Board members is established;
- which of its Board members are deemed independent and which are not;
- any material relationships Board members have with the company, its affiliates or their significant shareholders, as well as directorships and significant shareholdings in other companies.

Such disclosure is usually made on the company's website and in the annual report.

Each candidate for a Board position, and each Board member, has a duty to disclose to the company all information requested by the company or otherwise relevant to the evaluation of their formal independence. Candidates must disclose such information prior to their appointment, while Board members must update it (i) upon their appointment, (ii) at regular intervals to enable regular (re-)evaluation of formal independence, and (iii) upon a change of circumstances (e.g. a Board member's engagement in a new business or the occurrence of new private or business relationships).

It is good practice to appoint independent directors to the Board's audit, risk, remuneration and nomination committees, and to have them chair such committees.

More information on formal independence criteria and the appointment of independent Board members can be found in international guidance and in the Baltic corporate governance codes.[5]

KEY TAKEAWAYS

A. The Board provides strategic leadership and oversight; its purpose is the sustainable success of the company. The Board's duty is owed to the company, and the interests of shareholders and stakeholders are derived from it.

B. Each member individually, and the Board as a whole, owe fiduciary duties: the duty of care (acting within the law and the mandate, and making informed decisions to the standard of a prudent executive) and the duty of loyalty (putting the company first, disclosing conflicts, keeping confidentiality and never using information for personal gain).

C. The Board's responsibilities span purpose and strategy, resources and structure, long-term value, the governance framework, business plans and performance, oversight of management including appointment and succession of the CEO, control, risk, compliance and audit, reporting and disclosure, reputation and ethics, stakeholder relationships, committees and the Board's own evaluation.

D. Each Board member must prepare for, attend and actively participate in meetings, vote, keep developing their knowledge, and comply with the law, the Articles of Association and the Board charter.

E. The Chair leads the Board and is its link to management through the CEO, but is not the members' superior. The Chair sets the tone at the top, manages information flow, agendas and meetings, fosters open debate, oversees evaluation and succession, and communicates the Board's views together with the CEO.

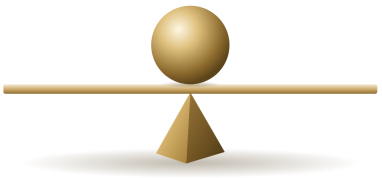
F. Executive and non-executive directors have the same duties, but only non-executive directors can truly challenge management. Boards should have as many non-executive members as possible and, among them, as many independent members as possible.

G. Formal independence means no material relationship with the company, its affiliates, their management or significant shareholders. The company should adopt and disclose its independence criteria and policy, assess independence before nomination, on appointment and regularly thereafter, and have independent directors serving on and chairing the key committees.

5 OECD (2023), G20/OECD Principles of Corporate Governance; Commission Recommendation 2005/162/EC of 15 February 2005 on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board; International Finance Corporation, IFC Corporate Governance Methodology; The Corporate Governance Code for the Companies Listed on Nasdaq Tallinn; Good Corporate Governance Recommendations for Companies in Latvia; The Corporate Governance Code for the Companies Listed on Nasdaq Vilnius.

QUESTIONS FOR THE BOARD

1. *Do all Board members understand that their duty is owed to the company, and how do we handle situations where the interests of shareholders or stakeholders diverge from it?*
2. *Do we meet the standard of a prudent executive: sufficient information, assumptions examined, alternatives considered and expert advice obtained where needed?*
3. *Do members disclose conflicts of interest and outside interests promptly, and do we record and manage them properly?*
4. *Which of the Board's responsibilities, from purpose and strategy to control, disclosure and self-assessment, receive too little of our time, and why?*
5. *Does the Chair ensure relevant, accurate and timely information, well-run meetings, open debate and a clear working relationship with the CEO?*
6. *Do we have enough non-executive and independent members to challenge management effectively, and do independent directors serve on and chair the audit, risk, remuneration and nomination committees?*
7. *Have we adopted and disclosed our formal independence criteria and policy, and when did we last assess the independence of each member?*
8. *Do we honestly assess our own performance, as a Board and as individual members, and act on the results?*



CHAPTER

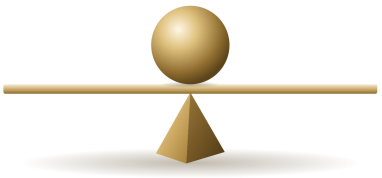
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KEY AREAS OF BOARD ENGAGEMENT

The six areas in which the Board's attention creates the most value: direction, control, integrity, innovation, leadership and accountability.

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CHAPTER

5.1

DIRECTION AND VALUE CREATION

How the Board sets the company's direction, oversees strategy and protects long-term value – and where its role ends and management's begins.

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5.1.1

COMPANY'S PURPOSE, VISION, MISSION AND VALUES

Before building the strategy, the Board should discuss with the shareholders what the purpose of the company is, and then set the vision, mission and values to provide clarity and direction for its employees, customers, stakeholders and the broader community. These elements serve as a foundation for the organisation's identity and guide its actions and decisions. There are numerous benefits for companies that have a well-established purpose, vision, mission and values, in particular:

- Clarity and focus: define and concentrate on long-term objectives.
- Guidance: support decision-making and strategy.
- Encourage purpose-driven business development.
- Inspire and motivate employees and attract top talent.
- Alignment: encourage collaboration and consistency.
- Competitive advantage: set the company apart from the competition.
- Improve branding and public relations through effective communication.
- Business sustainability: promote long-term growth.
- Resilience: navigate challenges based on purpose and values.
- Build public trust and reputation.
- Enable the company to have a broader and more meaningful impact on the world, beyond profit generation.

Purpose statement sets out the reason or reasons why an organisation exists. It defines the core reason for being and the positive impact the organisation wants to have on the world. The definition of the purpose leads to strategic choices and builds on cultural strengths to drive impact.

What is our purpose as an organisation, and how does it link with our "superpower", our capacity to make a distinctive contribution to the world?

Ask whether your purpose is:

1. Meaningful. In other words, does it make a real difference in people's lives? Does it have the potential to make a meaningful difference for all stakeholders?
2. Authentic. Does it match what people in the organisation care deeply about? Does it resonate with the company's values?

3. Credible. Does it draw on the organisation's unique abilities or assets? Can the company deliver in a way that makes a significant difference? Does it make business sense? Can it be translated into concrete actions?
4. Powerful. Are the needs the organisation addresses important and sizeable? How much good comes from addressing these needs?
5. Compelling. Is it clear, specific and aspirational enough to inspire and mobilise people both within and outside the organisation?

Examples of purpose statements:

- Telecommunication company: Inspire human progress through the power of communication and entertainment.
- Investment company: To help more and more people experience financial well-being.
- Beverage producer: Refresh the world. Make a difference.
- E-commerce company: To empower people and create economic opportunity for all.
- Automobile producer: To drive human progress through freedom of movement.
- Technology company: To create world-changing technology that enriches the lives of every person on earth.

Vision statement describes what the organisation will look like in the future: a big picture of what you want to achieve.

As you develop and review your vision statement, check for the following things:

1. Is it ambitious enough? The statement should feel aspirational, not like a finite goal to be accomplished.
2. Is it realistic enough? Make sure you strike a balance between the aspirational and the realistic.
3. Does it accurately reflect your organisation? Run the statement past internal stakeholders who were not involved in creating it, and ask for their feedback on what may be missing, which parts may be unnecessary, or how certain ideas may be phrased more effectively.
4. Does it make sense? Ask people outside the company to read the statement, to confirm that it makes sense to the average reader.

Examples of vision statements:

- Online technology company: To be Earth's most customer-centric company, where customers can find and discover anything they might want to buy online, and which endeavours to offer its customers the lowest possible prices.

- Financial services company: To become essential to our customers by providing differentiated products and services to help them achieve their aspirations.
- Computing technology company: To make the best products on earth and to leave the world better than we found it.
- Web technology company: To bring the metaverse to life and help people connect, find communities and grow businesses.
- Entertainment streaming company: Becoming the best global entertainment distribution service.

Mission statement describes what an organisation does and for whom, and how the vision will be achieved. The organisation's function, target audience and value proposition are elements often mentioned in a mission statement. The mission is an action statement that usually begins with the word "to".
It is important for:

- motivating employees;
- inspiring customers;
- strategic planning;
- setting values.

Examples of mission statements:

- Seller of furniture and home products: To offer a wide range of well-designed, functional home furnishing products at prices so low that as many people as possible will be able to afford them.
- Mass media and entertainment company: To entertain, inform and inspire people around the globe through the power of unparalleled storytelling.
- Business social media platform: To connect the world's professionals to make them more productive and successful.
- Athletic footwear and apparel producer: To bring inspiration and innovation to every athlete in the world.
- Construction toy production company: To inspire and develop the builders of tomorrow.

Double-check the uniqueness of your statements. They should not be too general and should not fit too many organisations.

Values are very important because they serve as guiding principles that help to shape the culture and behaviour of the company. Values also provide a shared

understanding of what is important for the company and help to align employees' actions with the company's mission and goals. They provide a framework for decision-making: when employees understand the company's values, they can use them as a reference point when making choices and solving problems, which leads to better outcomes and a more predictable corporate culture. Clearly defined values can also attract and retain employees who share them.

When defining the company's values, take into consideration the following aspects:

- Involve employees at all levels of the organisation in the process
- Ensure that your company values align with your purpose, mission and vision
- Keep them simple and easy to remember and apply
- Make them actionable: it should be clear how employees can demonstrate these values in their daily work
- Lead by example: senior management should set a good example and embrace the company's values.

A company's values are not just a statement of what the organisation believes in; they are a strategic tool for shaping culture, behaviour and decision-making. Values play a vital role in creating a positive and effective work environment and are a key component of an organisation's overall identity and success.

These statements are one of the primary starting points for the development of the strategy. They should be reviewed at the beginning of each strategy revision and amended if needed.

KEY TAKEAWAYS

A. Purpose, vision, mission and values are the foundation of strategy and of the company's identity. The Board should agree the purpose with the shareholders and then set the vision, mission and values before the strategy is built.

B. A purpose statement explains why the company exists; it should be meaningful, authentic, credible, powerful and compelling. A vision describes what the company will look like in the future; a mission describes what it does, for whom and how the vision will be achieved.

C. Values are a strategic tool, not a poster: they guide decisions and behaviour, shape culture and attract people who share them. They work only if they are simple, actionable, developed with employees and visibly practised by senior management.

D. The statements must be specific to the company; if they would fit any organisation, they are not doing their job. They should be reviewed at the start of every strategy revision and amended where needed.

QUESTIONS FOR THE BOARD

1. *Have we, together with the shareholders, agreed a purpose that explains why the company exists, and do our vision, mission and values follow from it?*
2. *Would our purpose, vision and mission statements fit almost any company, or do they clearly describe ours?*
3. *Were employees involved in defining the values, and can they say how the values apply to their daily work?*
4. *Does senior management visibly live the values, and does the Board see evidence of this in decisions, not only in communications?*
5. *When did we last review these statements against the strategy, and what changed as a result?*

5.1.2

CORPORATE CULTURE AND TONE AT THE TOP

Corporate culture is the pattern of behaviours that people in the organisation actually follow when no one is watching – how decisions are made, how bad news travels, how rules are applied when they are inconvenient. Tone at the top is the signal the Board and executive management send about which behaviours are rewarded, tolerated or punished. The two are inseparable: culture rarely rises above the standard that its leaders visibly practise. Policies, codes of conduct and training matter, but employees watch what leaders do far more closely than what they publish. A single decision – a sales target met by cutting corners and celebrated anyway, a senior manager whose misconduct is quietly overlooked – can undo years of compliance messaging.

Culture is not a soft topic to be delegated to the human resources function. It is a governance matter, because most corporate failures – fraud, safety incidents, mis-selling, sanctions breaches – are cultural failures first and control failures second. The controls existed; people chose to work around them, and leadership signalled, deliberately or not, that this was acceptable.

What the Board should do

Board actions:

1. Define, together with management, a small number of core values and expected behaviours, and approve the code of conduct that expresses them. Keep the language concrete: “we escalate bad news within 24 hours” is more useful than “we act with integrity”.
2. Model the behaviour personally. Arrive at Board meetings prepared, declare conflicts of interest without being prompted, challenge the CEO respectfully but openly, and observe the same rules that apply to employees – including expense discipline and training requirements.
3. Make culture a standing item, not a crisis item. Review cultural indicators at least annually: employee engagement and exit survey results, whistleblowing report volumes and outcomes, staff turnover in control functions, audit findings on behavioural root causes, and disciplinary statistics broken down by seniority.
4. Test consistency between incentives and values. Ask whether the remuneration system rewards the behaviours the code of conduct describes – or quietly rewards their opposite. Ensure that how targets are met carries real weight in performance evaluation, not only whether they are met.

5. Insist on consequence management at all levels. Verify that misconduct by senior or high-performing individuals is investigated and sanctioned with the same rigour as misconduct by junior staff. Nothing corrodes culture faster than visible double standards.
6. Get beyond the boardroom. Visit sites, meet middle managers and employees without executives present, and hear directly from the heads of internal audit, compliance and risk in closed sessions.

Warning signs

- Consistently positive reporting – no bad news, no near-misses, no dissent recorded in minutes.
- A dominant CEO whom no one, including directors, visibly challenges.
- High turnover in the finance, compliance, internal audit or legal functions.
- Whistleblowing channels that receive almost no reports – silence usually signals fear, not virtue.
- “Star performer” exceptions: targets, rules or investigations applied selectively to protect key revenue generators.
- Values posters on the walls that employees quote with irony rather than conviction.

Common pitfalls and drawbacks

Boards most often fail on culture in one of three ways. The first is delegation by declaration: approving a values statement and assuming the work is done. Culture is shaped by thousands of daily decisions, not by a document. The second is measurement theatre: tracking engagement scores as an end in themselves, which invites gaming and tells the Board little about how people behave under pressure. Indicators are prompts for inquiry, not proof of health. The third is inconsistency at the top itself: a Board that tolerates its own late papers, undeclared conflicts or dominant personalities has no credibility demanding better from management. Board members should also be alert to the opposite risk – a culture programme so heavy with surveys, campaigns and slogans that it breeds cynicism. Fewer, more honest signals outperform elaborate programmes.

KEY TAKEAWAYS

A. Culture is what people actually do when no one is watching; tone at the top is the signal the Board and management send about which behaviours are rewarded, tolerated or punished. Culture rarely rises above the standard its leaders visibly practise.

B. Culture is a governance matter, because most corporate failures are cultural failures first and control failures second. It should be a standing Board item, reviewed through concrete indicators, not a crisis item.

C. The Board shapes culture by defining a few concrete values and behaviours, modelling them personally, testing that incentives reward the right behaviours and insisting on consequence management at every level, including senior and high-performing individuals.

D. Governance professionals translate tone into practice: the company secretary keeps culture on the agenda, compliance makes the code and whistleblowing channels usable, internal audit reports cultural root causes, and HR aligns recruitment, promotion and pay with the stated values.

QUESTIONS FOR THE BOARD

1. *Do our stated values translate into a short, concrete code of conduct that employees can actually apply?*
2. *Does the Board itself observe the standards it expects of management, in preparation, conflicts of interest and open challenge?*
3. *Which cultural indicators do we review each year, and what did the last review tell us about the gap between stated values and daily practice?*
4. *Does our remuneration system reward how targets are met, not only whether they are met?*
5. *Is misconduct by senior or high-performing individuals investigated and sanctioned with the same rigour as misconduct by junior staff?*
6. *When did Board members last meet employees and middle managers without executives present, or hear from the heads of internal audit, compliance and risk in a closed session?*
7. *If an employee saw a Board member or the CEO breaching our code of conduct, would they dare to report it, and to whom?*
8. *When did we last decline a profitable opportunity on values grounds, and did we communicate that decision internally?*
9. *How quickly does bad news reach the Board, and does anyone soften it on the way?*

5.1.3

THE STRATEGY CYCLE: BUILDING, UPDATING, IMPLEMENTING

Strategy is the way in which the company uses its mission to achieve its vision, based on its values and on a clear understanding of the company's purpose and the expectations of the shareholders. The Board has to ensure that all the steps of the process listed below are implemented. Management develops and proposes the strategy and implements it once approved; the Board sets the direction, challenges the proposals, approves the strategy and oversees its implementation. The process below sets out the steps in three phases: development, approval and cascade, and implementation oversight.

Phase A – Strategy development or updating

1. **Agree the process and the roles.** Before any analysis begins, the Board and management should agree who does what, the strategy horizon (typically five to ten years), the timetable and the working format (for example, dedicated strategy sessions or an off-site meeting).
2. **Confirm purpose, mission, vision and values.** The strategy must flow from what the company exists to do and what it aspires to become. If these foundations are outdated or unclear, revisit them first – otherwise the strategy will lack an anchor and discussions will not be consistent.
3. **Map and understand the stakeholders.** Identify the company's key stakeholders and assess their relative power, interest and expectations and agree how conflicting expectations will be reconciled over time. Understanding the stakeholder map is the basis of effective strategy, and a strategy that lacks the buy-in of key stakeholders is unlikely to succeed.
4. **Conduct a thorough strategic analysis.** Analyse the company and its environment from the inside out, using recognised tools such as SWOT, PESTEL, VRIO, Ansoff Matrix, value chain analysis, Porter's five forces and gap analysis, and others that may be relevant for the company. Invite external experts where the in-house perspective is too narrow. Weak analysis at this stage is the most common root cause of later implementation failure.
5. **Identify and assess risks, and set the risk appetite.** Every strategic initiative carries risks, and these change over time. The Board should ensure that key risks are identified, assessed and matched with mitigation measures, and should define the risk appetite within which the strategy must fit. Without this, the result is a "fair-weather strategy" that works only until the first storm. The

Board should also distinguish the company's risk appetite from its risk capacity – the ability to absorb shocks – and pay particular attention to high-impact, low-probability risks, which are often neglected precisely because they seem unlikely to materialise.

6. **Evaluate industry trends, innovation and disruption.** The Board should consider the latest industry developments, technological change, research and development, and actual or potential disruptions to the business model – both as threats and as sources of opportunity.
7. **Integrate sustainability and ESG matters.** Sustainability-related risks and opportunities – including those identified through the double materiality assessment under CSRD/ESRS, where applicable – should be embedded in the company strategy itself, not treated as a separate strategy document. Further guidance on ESG topics is given in the BICG ESG Guidelines for Baltic Boards and the ecoDa ESG Governance Toolkit.[6]
8. **Develop and debate strategic options.** Crystallise realistic strategic opportunities and alternatives, and test them through scenario planning and stress-testing. Each option rests on certain assumptions. It is the Board's duty to challenge assumptions wisely, because assumptions presented by management carry built-in bias. Challenge contributes to the improvement of the strategy. A strategy adopted without genuine alternatives on the table has not been chosen – it has been assumed.
9. **Make the strategic choice.** Decide which alternatives will be embedded in the company strategy, using explicit criteria: value creation, fit with the risk appetite, available resources and competences. Record which options were rejected and why – this discipline will be valuable when the strategy is next reviewed.
10. **Translate the strategy into goals, objectives and action plans.** Ensure a clear hierarchy:
    - **Goals** – what needs to be accomplished to implement the strategy;
    - **Objectives** – specific, measurable milestones with a timeline for achieving each goal (the SMART criteria apply);
    - **Action plans** – how the company will achieve each objective, with named owners, resources and deadlines.
11. **Align resources and incentives with the strategy.** Verify that the budget, capital allocation, financing and people actually support the strategic priorities,

6 BICG (2022), ESG Guidelines for Baltic Boards – What, Why and How, https://www.bicg.eu/wp-content/uploads/2022/09/ESG-Guidelines-for-Baltic-Boards.pdf; ecoDa (2019), ESG Governance Toolkit for Boards, https://ecoda.eu/wp-content/uploads/2019/08/ESG-Governance-toolkit-for-boards_FINAL.pdf.

and link executive remuneration and key performance indicators (KPIs) to the strategic objectives.

Phase B – Approval and cascade

1. **Approve the strategy at Board level.** The Board formally approves the strategy together with its strategic goals, the implementation roadmap and the reporting schedule. Approval should follow genuine challenge and debate, not a single presentation.
2. **Ensure each unit's contribution is defined.** Cascade the strategy so that every business unit has its own sub-strategy (functional strategy) and knows its specific contribution to implementation, reflected in unit-level plans and individual objectives. Cascading does not mean that the creation of strategy is top-down: engagement is an iterative process, and each unit should be given the opportunity to work out what the strategy means for its own work that contributes to the company's objectives – this builds ownership as well as alignment.
3. **Communicate the strategy thoroughly.** Communicate the strategy and its rationale consistently within the company and, where appropriate, its essential parts to external stakeholders. People cannot implement what they do not understand. Boards routinely underestimate how much communication is needed – as a rule of thumb, double what seems sufficient, and then double it again. A concise "strategy on a page", built around a small number of clear strategic themes, is often far more effective than a lengthy strategy document.

Phase C – Oversight of implementation

1. **Assess the company's capability to implement.** A well-implemented average strategy will outperform a perfectly designed strategy that is poorly executed. The Board should periodically assess the organisation's implementation capability across dimensions such as people, organisational structure and resources, understanding of the business case, communication, measures, culture and processes.
2. **Monitor implementation through efficient reporting.** Management reports regularly against the approved KPIs and milestones; the Board reviews progress at an agreed cadence using a concise dashboard that includes leading indicators, not only financial results. Strategy should have a standing place on the Board agenda (2–4 times a year), not appear once a year.
3. **Take corrective action and review the strategy regularly.** Where implementation deviates from plan, the Board ensures that management analyses the causes and adjusts the actions – or, where the environment has

shifted, that the strategy itself is revised. A full strategy review should take place at least annually, and immediately after any material change in the business environment.

Strategy-setting process: Board and management roles

Often it is not clear to companies what the roles of the Board and management are in strategy development. One common failure is when the Board “rubber-stamps” the strategy: management prepares a 150-page strategy document, the Board discusses it for a few hours, and approves it. Another common failure is the “management Board”, where the Board engages itself in designing products, selecting markets, and developing implementation initiatives – effectively doing the job of executives.

There should be a clear division of responsibilities in strategy development: the Board owns the strategic direction, choices, desired outcomes and risk appetite, while management owns the analysis, development of strategic options, resource and capability planning, and execution of the chosen strategy.

The five stages below put this division into practice, alternating lead responsibility between the Board and the executives, so that strategy is set through structured dialogue rather than by either party alone.

STAGE	PRIMARY ROLE	WHAT HAPPENS
1. Strategic framing	**Board**	Board discusses and (re)approves purpose, vision, mission and values, clarifies the expectations of owners, shareholders and other key stakeholders, and sets the ambition, key strategic issues, risk appetite and the questions the strategy must answer. Where a strategy committee exists, it prepares this discussion for the full Board.
2. Analysis & options	**Executives**	Management conducts internal and external analysis (market, competitive, financial and risk) and develops credible strategic alternatives, including underlying, financial implications, risks, trade-offs and how each option addresses the Board's strategic questions. Where useful, scenario planning is used to stress-test alternatives against plausible future conditions.
3. Strategic choice	**Board**	Management presents the strategic alternatives. The Board challenges assumptions, tests trade-offs and, after a thorough discussion, selects the preferred strategic direction(s). The Board's rationale and any conditions attached to the decision are recorded in the minutes to provide a clear mandate for the next stage.
4. Strategy development	**Executives**	Management converts the chosen direction into an integrated strategy: objectives, key performance indicators, initiatives, resource allocation, capabilities, financial plans, risk mitigation measures and an implementation roadmap with clear ownership and milestones.

STAGE	PRIMARY ROLE	WHAT HAPPENS
5. Approval & oversight	**Board**	Board assesses whether the resulting strategy reflects the agreed choices and risk appetite, formally approves it, and thereafter oversees execution through periodic progress reviews against the agreed KPIs and milestones. Material deviations, changing conditions or emerging risks are escalated to the Board, which revisits Stage 1 as needed – making strategy-setting a continuous cycle rather than a one-off event.

Warning signs

- The Board is presented with only one strategic proposal, rather than alternative strategic options and their trade-offs.
- Strategy papers are always approved without challenge or amendment – silence is being mistaken for consent, a classic symptom of groupthink.
- The strategy appears on the Board agenda only once a year, at approval time.
- Unit managers cannot explain their unit's contribution to the strategy.
- Reporting on implementation consists of financial results only, with no leading indicators.
- Sustainability is handled in a separate document that never intersects with the company strategy.
- The assumptions behind the strategy are never revisited once it has been approved.
- No one can say in advance what would cause the Board to reopen the strategy.

KEY TAKEAWAYS

A. Strategy is set through structured dialogue between the Board and management: the Board frames the direction, ambition, risk appetite and questions; management analyses and develops credible options; the Board challenges assumptions and chooses between genuine alternatives; management develops the detailed strategy; the Board approves it and oversees implementation.

B. Strategy development rests on confirmed purpose, mission, vision and values, a clear stakeholder map, thorough analysis, a defined risk appetite (distinguished from risk capacity), attention to trends and disruption, and sustainability embedded in the strategy itself.

C. A strategy adopted without genuine alternatives on the table has not been chosen but assumed. Options should be tested through scenario planning and stress-testing, and rejected options recorded with the reasons.

D. Approval is not the end: the strategy must be translated into goals, objectives and action plans, aligned with budget, resources and incentives, cascaded to every unit and communicated far more than seems necessary.

E. Implementation should be monitored two to four times a year through a concise dashboard with leading indicators, with corrective action where needed and a full review at least annually or after any material change in the environment.

QUESTIONS FOR THE BOARD

1. *Have the Board and management agreed who does what in strategy-setting, the strategy horizon, the timetable and the working format?*
2. *Does the Board set the direction and risk appetite before management develops options, or does it react to a finished document?*
3. *Were genuine alternatives presented, and did we test the assumptions behind the option we chose?*
4. *Is the strategy translated into goals, objectives and action plans with named owners, and are budget and incentives aligned with it?*
5. *Can every unit manager explain their unit's contribution to the strategy?*
6. *How often does strategy appear on our agenda, what does our implementation dashboard show beyond financial results, and when did we last revise the strategy in response to a change in the environment?*
7. *Do we know which risks could break this strategy, and how they will be mitigated?*
8. *Which stakeholders must support this strategy for it to succeed, and how do we know that they do?*
9. *How quickly would we learn that implementation is going off track?*

5.1.4

INTEGRATING SUSTAINABILITY INTO COMPANY STRATEGY, ITS OVERSIGHT, SUSTAINABILITY REPORTING

Sustainability has moved from a peripheral corporate-responsibility function to a core input into strategy. Climate-related risk, resource dependency, workforce and supply-chain resilience, and stakeholder expectations now bear directly on a company's competitive position, cost of capital and even existence. For Boards, this means sustainability cannot be delegated to a sustainability officer, treated as an annual reporting exercise, or managed through a separate sustainability strategy: it must be part of the company's core strategy, set, approved and overseen through the same governance processes.

This holds regardless of whether a company falls within the scope of mandatory EU sustainability regulation. Lenders, investors, customers and supply-chain partners increasingly apply their own expectations, and the underlying business drivers – energy prices, physical climate risks, access to capital and talent – affect every company. The Board's task is not to maximise sustainability ratings, but to ensure that material sustainability factors are properly weighed in strategic decisions.

The role of the Board

Sustainability considerations belong at the stage of strategy development and annual revision, not bolted on after strategic choices have already been made or reduced to a year-end reporting exercise.

Integration of sustainability-related matters into company strategy, revision of business models, and oversight of these activities is getting more attention in boardrooms – and these topics have become even more important as new EU-level regulation, including CSRD, ESRS and CSDDD, has raised the stakes, even though the 2026 Omnibus I amendments narrowed mandatory reporting and due diligence to the largest companies. The Board should take leadership in re-evaluating risks, identifying new sustainability-related risks and opportunities, and reshaping strategy where needed, rather than waiting for management or auditors to surface them.

Sustainability-related issues do not only create obligations to comply with EU regulation and generate risk; they also open access to opportunities that might otherwise go uncaptured, including:

- New business models

- New products and offerings
- Access to green capital on more favourable terms
- Improved competitive advantage
- Reduced energy use, lowering dependence on energy markets and price volatility
- A stronger company brand

The Board's ongoing task is to challenge, approve and monitor: ensuring sustainability-related risks and opportunities are identified through a rigorous double materiality assessment, embedded in the chosen strategy, properly resourced, and reported accurately to the market. Its oversight does not stop at risk and opportunity either – the Board is also expected to act when sustainability management within the company reasonably deviates from the company's stated values.

What the Board should do

1. **Set the sustainability risk appetite** at the strategic framing stage, alongside financial and operational risk appetite, so it shapes strategic choice rather than following it.
2. **Require and challenge a double materiality assessment** – impact materiality (the company's effect on people and environment) and financial materiality (sustainability factors' effect on the company) – refreshed at least annually rather than treated as a one-off compliance exercise.
3. **Assign clear oversight,** either to the full Board or to a dedicated committee (audit, risk, or a standalone sustainability committee), with a defined mandate, reporting line and competence requirement.
4. **Approve measurable targets and KPIs** linked to the strategy – not generic commitments – and track them with the same rigour as financial KPIs in periodic Board reporting.
5. **Oversee the reporting process itself,** including data quality, internal controls and external assurance, for CSRD/ESRS-aligned disclosures where in scope, or proportionate voluntary reporting were not.
6. **Link executive remuneration,** where appropriate, to sustainability KPIs so management incentives align with the approved strategy.
7. **Build Board competence** through training, briefings or committee expertise, so Board members can test management's assumptions rather than defer to them.

8. **Extend oversight into the value chain,** given that suppliers, customers and lenders increasingly request sustainability data and due diligence regardless of a company's own regulatory scope.

Warning signs

- Sustainability strategy, targets or reporting owned entirely by one function, with no Board-level sponsor or committee.
- Public claims or reported KPIs that management – or the Board – cannot trace back to underlying data.
- A materiality assessment that has not changed in substance year on year, or was outsourced entirely with no internal ownership.
- Sustainability reporting produced after the strategy is finalised, rather than informing it.
- No independent assurance over reported sustainability data, or assurance scope quietly narrowing over time.
- Board papers that treat sustainability as a once-a-year agenda item rather than a recurring line in strategy and risk reporting.

Common pitfalls and drawbacks

- **Treating reporting as the objective.** Compliance with CSRD/ESRS, or a voluntary framework, is necessary but not sufficient – a well-reported strategy that does not reduce risk or build resilience has still failed its purpose.
- **Starting too late and under-resourcing the work,** compressing materiality and data-collection into a year-end scramble that degrades quality and invites audit findings.
- **Greenwashing through selective disclosure –** publicising favourable metrics while omitting less favourable ones – which exposes the company and its Board members to reputational and, increasingly, legal risk.
- **Passive Board oversight:** receiving sustainability updates without challenging data quality or the gap between stated ambition and actual resourcing.
- **Treating scope thresholds as the only test.** Following the EU's 2026 Omnibus simplification, direct CSRD scope has narrowed materially (broadly, large undertakings above 1,000 employees and €450 million net turnover); companies below that threshold can still face equivalent demands indirectly, as larger customers, lenders and investors request comparable data down the value chain.[7]

7 Thresholds under Directive (EU) 2022/2464 (CSRD) as amended by the EU "Omnibus I" simplification package adopted in 2025–2026.

- **Underinvesting in Board and management competence,** leaving oversight dependent on external advisers who cannot be held accountable in the way directors can.
- **Waiting for the rules to settle.** National transposition of CSRD is still evolving across Estonia, Latvia and Lithuania, which tempts companies to delay rather than build durable internal processes – a strategy built for the direction of travel, not just the current rules, tends to age better.

Practical, step-by-step guidance and the specific tasks for Boards related to ESG and sustainability can be found in the BICG ESG Guidelines for Baltic Boards, in ESG Governance: questions Boards should ask to lead the sustainability transition, and in A Practical Guide for Boards and Leadership Teams on Sustainability.[8]

KEY TAKEAWAYS

A. Sustainability is a core input to strategy, not a separate reporting exercise. It bears on competitive position, cost of capital and resilience, and it must be integrated into the company's strategy through the same governance processes as any other strategic matter.

B. The Board's role is oversight, starting at strategy development: setting the sustainability risk appetite, requiring and challenging a double materiality assessment, assigning clear oversight, and approving measurable targets and KPIs linked to the strategy.

C. Sustainability creates opportunities as well as obligations: new business models and products, access to green capital, competitive advantage, lower energy dependence and a stronger brand.

D. The Board oversees the reporting process itself, including data quality, internal controls and external assurance, and should be alert to greenwashing through selective disclosure.

E. Companies outside the direct scope of CSRD can still face equivalent demands through customers, lenders and investors, so processes should be built for the direction of travel, not only the current rules.

8 BICG (2022), ESG Guidelines for Baltic Boards – What, Why and How, https://www.bicg.eu/wp-content/uploads/2022/09/ESG-Guidelines-for-Baltic-Boards.pdf; ESG Governance: questions Boards should ask to lead the sustainability transition; BICG (2022), A Practical Guide for Boards and Leadership Teams on Sustainability, https://www.bicg.eu/wp-content/uploads/2022/01/A-practical-guide-for-boards-leadership-teams-on-sustainability-11.pdf.

QUESTIONS FOR THE BOARD

1. *Where in our strategy process do sustainability risks and opportunities enter, and is that before or after the main strategic choices are made?*
2. *Who owns our double materiality assessment, when was it last refreshed, and which external stakeholders were consulted?*
3. *Do we have measurable sustainability targets and KPIs linked to the strategy, and are they tracked with the same rigour as financial KPIs?*
4. *Which of our reported sustainability metrics are independently assured, and can we trace every public claim to underlying data?*
5. *Does the Board have the competence to test management's assumptions on sustainability, or do we defer to external advisers?*
6. *How exposed are we, directly or through our value chain, to CSRD, taxonomy or due-diligence requirements, and how is that changing?*
7. *What are our two or three most material sustainability-related risks and opportunities, and how do they change our strategy, not just our reporting?*
8. *Are our public sustainability commitments and targets consistent with what management is actually resourcing and delivering?*
9. *Does management's remuneration reward the sustainability outcomes we say we want, and what escalation path exists if a target is missed or a material risk emerges mid-cycle?*

5.1.5

CAPITAL STRUCTURE AND DIVIDEND POLICY

How a company finances itself – the mix of debt and equity it carries – and how it returns capital to shareholders are not routine treasury matters. Together they determine a company's resilience under stress, its capacity to fund strategy and growth, its cost of capital, and the confidence lenders, investors and rating agencies place in it. Capital structure and dividend policy sit directly within the Board's fiduciary oversight: decisions here are strategic choices with legal consequences, not calculations to be left entirely to the finance function.

The role of the Board

The Board's task is to set the framework within which capital structure and distribution decisions are made, and to test management's proposals against it – not to draft them. In practice, this means approving a target capital structure and a dividend policy consistent with the company's strategy and risk appetite.

Usually, the final decision to distribute profit rests with the general meeting of shareholders, acting on the approved annual accounts and the proposal of the Board. That does not reduce the Board's role to a formality. The Board reviews and approves the management's dividend proposal before it reaches shareholders. Either way, the Board's job is to confirm that a proposed distribution is lawful, that it does not compromise the company's solvency or its ability to fund strategy, and that it is consistent with a policy the Board has itself endorsed – rather than an ad hoc figure produced late in the reporting cycle.

What the Board should do

1. **Set and periodically review a target capital structure** – an acceptable range for leverage and the debt/equity mix – aligned with the company's risk appetite and strategy, not simply the lowest available cost of capital or short-term tax optimisation.
2. **Approve a clear, published dividend policy** (a payout ratio range and a stated priority between reinvestment, deleveraging and shareholder returns) so that distributions follow a discipline the Board has set, rather than being decided year to year. The dividend policy also plays an additional role: it explains transparently to the shareholders and all relevant stakeholders how dividends are set. This is particularly important where some shareholders demand high dividends without regard to the financial health of the company.

3. **Verify the statutory distribution tests** before recommending any dividend to shareholders. Estonian law requires that equity remain at least half of share capital and that a distribution not endanger solvency; Latvian law prohibits distribution if own funds would fall below share capital; Lithuanian law restricts distribution that would reduce equity below authorised capital or mandatory reserves. These are Board-level checks, not back-office formalities.[9]
4. **Stress-test the capital structure** against adverse scenarios – a revenue shock, a rise in interest rates, tighter refinancing terms, or a market unwilling to roll over debt – rather than relying solely on the base case.
5. **Assess covenant headroom and refinancing risk** before approving new borrowing or a distribution that would reduce that headroom, and monitor both on an ongoing basis, not only at renewal.
6. **Maintain a predictable, well-communicated policy,** particularly for companies listed on Nasdaq Baltic, where unexplained deviation from stated dividend guidance affects market credibility and share price.
7. **Record the rationale** for capital structure and dividend decisions in Board and shareholder minutes, including the basis for the distributable-profit calculation – closing the same accountability gap this Handbook flags for strategic decisions generally.

Warning signs

- A dividend maintained or increased despite weakening cash flow, rising leverage or narrowing covenant headroom.
- No clearly articulated capital structure or dividend policy – distributions and financing decided ad hoc, year to year, with little Board discussion.
- Distributions approved without documented confirmation that statutory solvency and net-asset tests were met.
- Growing reliance on short-term or refinancing debt to fund distributions or ongoing investment.
- Capital structure decisions driven primarily by tax optimisation, with limited regard to underlying business risk.
- Little or no Board challenge to management's proposed leverage, payout ratio or financing structure.

9 See the provisions on the distribution of profit and the protection of capital in the Estonian Commercial Code, the Latvian Commercial Law and the Lithuanian Law on Companies.

Common pitfalls and drawbacks

- **Treating dividend policy as a technical finance decision,** delegated entirely to the CFO and rubber-stamped by the Board rather than scrutinised as a strategic choice.
- **Protecting a stable or progressive dividend at the expense of strategic investment,** including transition or resilience-related capital expenditure, weakening the company's longer-term position to preserve a short-term signal to the market.
- **Carrying leverage inconsistent with the business's actual risk profile,** either too conservative to fund growth or too aggressive relative to the volatility of the underlying business.
- **Overlooking the statutory distribution tests,** which in each Baltic jurisdiction can expose Board members to personal liability for an unlawful distribution – this is a compliance matter, not only a financial one.
- **An inconsistent or opportunistic dividend policy** that damages market credibility and, for listed companies, raises the cost of capital by increasing perceived uncertainty.
- **Ignoring the tax asymmetry across the Baltic states** when structuring group financing and dividend flows – moving cash between an Estonian or Latvian entity, where reinvested profit is untaxed, and a Lithuanian parent taxed annually, without coordinated group tax planning.
- **Failing to document the Board's reasoning,** leaving no audit trail for why a particular capital structure or distribution was approved – a gap that becomes costly precisely when a decision is later questioned.

As elsewhere in this Handbook, the mechanism of approval differs by structure – the Supervisory Board or Council in the two-tier structures common across Estonia, Latvia and Lithuania, or the non-executive members of a one-tier Board – but the standard does not: a disciplined, documented policy, tested against the law and the company's own risk appetite, before it ever reaches the shareholders who make the final call.

KEY TAKEAWAYS

A. Capital structure and dividend policy are strategic choices with legal consequences, not routine treasury matters. They determine the company's resilience, its capacity to fund strategy and its cost of capital.

B. The Board sets the framework, a target capital structure and a published dividend policy aligned with strategy and risk appetite, and tests management's proposals against it. The final decision on distributions usually rests with the shareholders, acting on the Board's proposal.

C. Before recommending any distribution, the Board must verify the statutory tests in the relevant Baltic jurisdiction; an unlawful distribution can expose directors to personal liability.

D. The different tax treatment of retained and distributed profit in Estonia, Latvia and Lithuania should inform where cash is held and how intra-group distributions are structured.

E. The capital structure should be stress-tested against adverse scenarios, covenant headroom and refinancing risk monitored continuously, and the rationale for every decision recorded in the minutes.

QUESTIONS FOR THE BOARD

1. *Do we have an approved target capital structure and a published dividend policy, and when were they last reviewed against the strategy and risk appetite?*
2. *Is the current dividend proposal consistent with that policy, and if it deviates, has the Board recorded why?*
3. *Who verified that the statutory solvency and minimum-equity tests are met for this distribution, and is that verification documented?*
4. *How would our leverage and liquidity hold up under a revenue shock, higher interest rates or a tighter refinancing market?*
5. *Are we retaining enough capital to fund the strategy without becoming dependent on external financing?*
6. *Does our group financing and distribution structure take account of the differing tax treatment of profit across the Baltic states?*
7. *What is our target leverage range, and why is it the right one for our strategy and risk appetite, not simply the cheapest available financing?*
8. *What covenant headroom do we have today, and how does this financing or distribution decision change it?*
9. *If a lender or rating agency reviewed our capital structure today, what would concern them most?*

5.1.6

MERGERS, ACQUISITIONS AND MAJOR TRANSACTIONS

Few decisions test a Board as severely as a merger, an acquisition, a disposal of a core business or another transformational transaction. The amounts at stake are large, the information is asymmetric, the timetable is compressed, and the atmosphere is often charged with ambition. Research consistently shows that a substantial share of acquisitions destroy value for the buyer – not because the idea was bad, but because the price was too high, the risks were underestimated or the integration failed. The Board's role is therefore not to run the deal, but to ensure that the company enters it for the right reasons, at a defensible price, with open eyes and with a credible plan for what happens after signing.

Major transactions also concentrate governance risks that are diffuse in ordinary business: conflicts of interest, related party transactions, insider information, disclosure obligations and shareholder rights all converge on a single decision. In smaller markets, where the counterparty may well be connected to a shareholder or a director, this convergence deserves particular attention.

The role of the Board

The Board owns three things in any major transaction: the strategic rationale, the approval decision and the oversight of execution. Management identifies opportunities, negotiates and integrates; advisers value, structure and document. The Board's distinct contribution is disciplined judgement – whether the transaction serves the company's strategy or merely someone's ambition, whether the price rests on realistic assumptions, and whether the organisation can absorb what it is buying. The Board must also safeguard process integrity: conflicts of interest, inside information, equal treatment of shareholders, and disclosure and merger control requirements.

What the Board should do

Board actions:

1. Anchor every transaction in strategy before discussing price. Require management to show how the deal fits the approved strategy and what the realistic alternatives are – including organic growth, partnership or doing nothing.
2. Establish the process at the outset: a clear mandate for management, approval thresholds, a timetable for Board involvement, and rules for confidentiality and

insider lists. For significant deals, consider a transaction committee of unconflicted Board members with relevant experience.

3. Identify and manage conflicts of interest immediately. Require every Board member and senior executive to declare any connection to the counterparty, its owners or its advisers. Conflicted Board members must be excluded from deliberation and decision, and related party transaction procedures must be applied where the law or the company's corporate governance code requires.
4. Commission genuinely independent advice. Ensure that financial, legal and tax due diligence is proportionate to the deal, and consider an independent fairness opinion on valuation – especially where a shareholder, a director or management has an interest in the outcome.
5. Interrogate the assumptions, not only the model. Ask which synergies are proven, which are hoped for, and what the deal looks like if revenue synergies are removed entirely. Require a downside case and a walk-away price, and hold the Board to it when negotiation pressure mounts.
6. Approve the integration plan together with the deal, not after it. Require named accountability for integration, a budget for one-off costs, retention plans for key people of the target, and milestones the Board will track.
7. Review the outcome. Twelve to twenty-four months after closing, compare actual performance against the investment case presented at approval, and record the lessons for the next transaction.

Warning signs

- Deal momentum: the transaction accelerates while scrutiny weakens, and the question shifts from "should we" to "how fast can we".
- A CEO personally invested in the deal as a legacy project, with the Board hearing only supporting evidence.
- Due diligence findings dismissed as "deal points" without analysis of their long-term cost.
- Advisers remunerated only on completion, with no one in the room paid to say no.
- Undeclared connections between the counterparty and shareholders, Board members or executives.
- No integration plan, budget or named owner at the moment of approval.

Common pitfalls and drawbacks

The most expensive pitfall is overpayment driven by momentum and optimism: once time, money and reputation have been invested in a deal, walking away feels

like failure, and Boards approve prices they would have rejected at the outset. The second is treating approval as the finish line – most value is won or lost in integration, which begins the day after closing and typically takes years. The third is process failure: a conflicted Board member who participated in the decision, a missed disclosure, a breach of insider rules or an overlooked merger control filing can invalidate the transaction and expose Board members to personal liability. Boards should also recognise the drawbacks of excessive caution: a Board that demands certainty on every point will lose good opportunities to faster competitors. The aim is disciplined speed – a well-designed process that allows the Board to decide quickly without skipping the questions that matter.

Guidance for other governance professionals

Company secretaries, general counsel, chief financial officers and internal auditors carry much of the practical burden of a clean transaction. The company secretary should design the decision trail: properly convened meetings, complete papers, minutes recording the alternatives considered and the reasons for the decision, declarations of interest, and insider lists maintained from the first confidential discussion. General counsel should map the approval requirements early – shareholder approvals, related party transaction procedures, merger control filings, disclosure obligations – and build them into the timetable. The chief financial officer should present the investment case with its assumptions visible and testable, including a downside scenario, and resist pressure to tune the model to a predetermined answer. Internal audit should review the process after closing. The guiding principle for all of these roles: the file should show that the Board decided carefully, on complete information and free of conflicts.

KEY TAKEAWAYS

A. Major transactions test a Board more severely than any other decision: large amounts, asymmetric information, compressed timetables and charged ambition. A substantial share of acquisitions destroy value because the price was too high, the risks underestimated or the integration failed.

B. The Board owns the strategic rationale, the approval decision and the oversight of execution. Management negotiates and integrates; advisers value and document. The Board's contribution is disciplined judgement and process integrity.

C. Every transaction should be anchored in strategy before price is discussed, run under a clear process with approval thresholds and insider rules, and protected against conflicts of interest through declarations and exclusion of conflicted Board members.

D. Independent advice, interrogated assumptions, a downside case and a walk-away price protect against deal momentum. The integration plan, with named accountability and a budget, is approved with the deal, not after it.

E. Outcomes should be reviewed twelve to twenty-four months after closing against the investment case, and the lessons recorded.

QUESTIONS FOR THE BOARD

1. *Do we have a defined process for major transactions: mandate for management, approval thresholds, Board timetable, confidentiality and insider lists?*
2. *Has every Board member and senior executive declared any connection to the counterparty, its owners or its advisers, and have conflicted Board members been excluded?*
3. *Is our due diligence and valuation advice genuinely independent, and have we seen a downside case and set a walk-away price?*
4. *Is there a named owner, a budget and milestones for integration at the moment of approval?*
5. *Are our advisers paid in a way that gives someone an incentive to say no?*
6. *When did we last compare a completed transaction against its investment case, and what did we learn?*
7. *Why this target, why now, and what happens to our strategy if we do not proceed?*
8. *What did due diligence find that we are choosing to accept, and why?*
9. *If this transaction appeared on the front page tomorrow, could we explain the process and the price with confidence?*

5.1.7

BUDGET AND KPIS FOR THE COMPANY AND CEO, PERFORMANCE MONITORING AND EVALUATION

When targets are defined, the Board must set specific KPIs or other agreed performance measures for the company and for the CEO, monitor regularly (at least quarterly) how management is performing against the set KPIs, and take the necessary measures if performance is not satisfactory. The more often the Board monitors performance, the more opportunities it will have during the year to take the measures needed to adjust operations and drive the company to better results.

KPIs should be both financial and non-financial (e.g. related to ESG and sustainability). It is not obligatory to set the same KPIs for the CEO as for the company. The CEO could have additional (e.g. “soft”) KPIs related to organisational culture and the well-being and satisfaction of employees.

It is good practice not to set too many KPIs. With more than 10 KPIs, the weight of a single KPI will be less than 10 per cent, and the motivation to achieve it may be weak.

KPIs should be defined very clearly and understandably, in order to avoid discussions after the year end about whether or not they have been achieved.

It is good practice to use the SMART concept when setting KPIs. Some companies use the SMARTER concept (specific, meaningful, achievable, relevant, time-bound, evaluate and readjust).

A budget sets out the income and expenses planned for the company. The budget should be challenging enough on both the income and the expense side. This gives management a sense of urgency, makes them continually search for the best and most innovative solutions and the most efficient way of operating, and keeps the company highly competitive. All these measures help to ensure that the value created is maximised.

KEY TAKEAWAYS

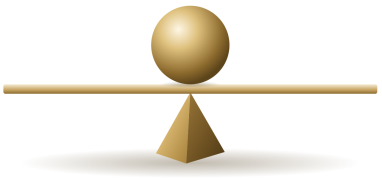
A. Once targets are set, the Board defines specific KPIs for the company and the CEO, monitors performance against them at least quarterly and takes corrective measures where performance falls short.

B. KPIs should be both financial and non-financial, few enough for each to matter (more than ten dilutes their weight), defined clearly enough to avoid year-end disputes, and SMART. The CEO's KPIs need not be identical to the company's and may include softer measures such as culture and employee well-being.

C. The budget should be challenging on both the income and the expense side, giving management a sense of urgency and keeping the company competitive and focused on value creation.

QUESTIONS FOR THE BOARD

1. *Do the company and the CEO have a short set of clearly defined, SMART KPIs, financial and non-financial, aligned with the strategy?*
2. *Is any KPI so weakly weighted that it no longer motivates, and are the definitions precise enough to leave no room for dispute at year end?*
3. *How often does the Board review performance against the KPIs, and what happened the last time performance fell short?*
4. *Is the budget challenging enough on both the income and the expense side, and how do we know?*
5. *Are the CEO's KPIs and remuneration consistent with the company's KPIs and with the behaviours we expect?*



CHAPTER

5.2

CONTROL, RISK AND ASSURANCE

How the Board makes sure that controls work, risks are understood and managed, and the company can withstand and recover from disruption.

IN THIS SECTION

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5.2.1

CONTROL ENVIRONMENT

The control environment of an organisation refers to the **collective attitude, awareness and actions** of the Board, management and employees towards internal controls. It establishes the **tone at the top** for the entire company's control system and influences how employees perform their duties.

A strong control environment is one in which employees understand their roles, act within their authority and are committed to doing things correctly. It is fundamental to a company's health and sustainability, supporting **risk management, operational efficiency, regulatory compliance and accountability**. Ultimately, it builds **confidence among the Board and shareholders** that the company can achieve its goals while protecting its assets and upholding ethical standards.

For the Board, an effective control environment provides greater confidence that the company is well managed, key risks are identified, financial and non-financial information is reliable, and decisions are implemented responsibly. For the company, it supports better performance, fewer surprises, stronger accountability and a more disciplined use of resources. For shareholders and other stakeholders, it strengthens trust that the company acts lawfully, ethically and in line with its long-term interests.

The control environment consists of several **connected elements**. These include the company's values, ethics and culture; clear roles and responsibilities; the organisational structure; the competence and integrity of management and employees; policies and procedures; risk management practices; internal controls; reporting and escalation mechanisms; and the work of internal audit, external audit and compliance functions where applicable. A good control environment is not only a set of documents or formal procedures. It is also about **how people actually behave**, how decisions are made, how issues are reported, and whether accountability is applied consistently across the company.

The Board and management have different but complementary responsibilities in ensuring an effective control environment.

The **Board is responsible** for setting expectations, approving key policies, overseeing risk management and internal control systems, challenging management, and regularly assessing whether the control environment remains appropriate for the company's size, complexity, strategy and risk profile.

Management is responsible for designing, implementing and operating the control environment in practice. This includes establishing procedures, assigning responsibilities, monitoring compliance, addressing weaknesses, and ensuring that employees understand and follow the expected standards.

The Board should not manage controls on a daily basis, but it must ensure that management takes this responsibility seriously and that the Board receives reliable information on material risks and control issues.

Establishing and improving an effective control environment requires clear tone from the top, well-defined responsibilities, risk-based policies and controls, competent people, reliable reporting, effective assurance, timely correction of weaknesses and continuous review as the company and its risks evolve.

Key steps in establishing and improving an effective control environment are:

1. **Set the right tone at the top**
   The Board and management should clearly communicate that integrity, accountability, risk awareness and compliance are expected in all decisions and behaviours.
2. **Define clear roles and responsibilities**
   The company should clearly allocate decision-making authority, approval rights, reporting lines and accountability between the Board, management, control functions and employees.
3. **Assess key risks and control needs**
   The company should identify the main strategic, financial, operational, compliance, sustainability and reputational risks, and determine what controls are needed to manage them effectively.
4. **Establish policies and procedures**
   Key areas such as finance, procurement, conflicts of interest, delegations of authority, risk management, compliance, data protection, whistleblowing and reporting should be covered by clear and practical policies approved by the Board.
5. **Ensure competent people and adequate resources**
   The company should have people with the necessary skills, experience and authority to operate controls, manage risks and report issues properly.
6. **Create reliable reporting and escalation channels**
   Management and the Board should receive timely, accurate and relevant information on risks, incidents, breaches, control weaknesses and corrective actions.

7. **Monitor how controls work in practice**
   Controls should not only exist on paper. Management should regularly test whether they are actually followed and whether they remain effective.
8. **Use internal audit, external audit and compliance functions effectively**
   Where appropriate, independent assurance should help the Board and management understand whether the control environment is reliable and where improvements are needed.
9. **Address weaknesses and follow up on actions**
   Identified control gaps, audit findings or incidents should lead to clear corrective actions, responsible owners and deadlines, with regular follow-up.
10. **Review and improve continuously**
    The control environment should be updated when the company grows, changes strategy, enters new markets, digitalises processes, faces new risks or operates under new regulation.

Several well-known tools and frameworks can help a company to establish and maintain a sound control environment. The most useful for Boards are the following:

- **COSO Internal Control Framework**. This provides a structured approach to internal control, covering the control environment, risk assessment, control activities, information and communication, and monitoring. It is one of the most widely used internal control frameworks.
- **Three Lines Model**. This clarifies the roles of management, the risk and compliance functions and internal audit in managing and assuring risks and controls. It helps the Board to understand who is responsible for what.
- **ISO 31000 risk management standard**. This provides principles and guidance for identifying, analysing, evaluating, treating, monitoring and communicating risks across the organisation.
- **Delegation of authority matrix**. This sets clear approval rights for key decisions, such as investments, contracts, hiring, financing, procurement and transactions with related parties. It reduces confusion and strengthens accountability.
- Corporate governance **policies** and other **documents**, such as the risk appetite statement, Board and committee charters, code of conduct, ethics policy, conflict of interest policy and register, risk register and internal control register, internal audit plan, and whistleblowing policy and mechanism.

More on internal control and risk management can be found in sub-chapters 5.2.2 and 5.2.3.

The **success of a strong control environment** depends on several practical factors:

- First, there must be a clear tone at the top: the Board and management should consistently demonstrate integrity, accountability and respect for rules;
- Second, responsibilities must be clear, so that people know who is authorised to decide, approve, monitor and report;
- Third, the company needs reliable information flows, including timely reporting of risks, incidents, control failures and corrective actions;
- Fourth, the control environment should be proportionate: it should support the business and decision-making, not create unnecessary bureaucracy.

Finally, it should be regularly reviewed and improved, especially when the company grows, changes strategy, enters new markets, faces new regulation or experiences significant incidents. A strong control environment is therefore not a one-time exercise, but a continuous governance discipline.

KEY TAKEAWAYS

A. The control environment is the collective attitude, awareness and behaviour of the Board, management and employees towards internal control. It sets the tone for the whole control system and shows in how people actually behave, not only in the documents.

B. The Board sets expectations, approves key policies, oversees risk management and internal control, challenges management and regularly assesses whether the control environment fits the company's size, complexity, strategy and risk profile. Management designs and operates the controls.

C. A sound control environment rests on tone at the top, clear roles and responsibilities, risk-based policies and controls, competent people, reliable reporting and escalation, effective assurance, timely correction of weaknesses and continuous review.

D. Recognised tools help: the COSO Internal Control Framework, the Three Lines Model, ISO 31000, a delegation of authority matrix and a coherent set of governance policies.

E. The control environment should be proportionate, supporting the business and decision-making rather than creating bureaucracy, and it should be reviewed whenever the company grows, changes strategy, enters new markets, faces new regulation or experiences a significant incident.

QUESTIONS FOR THE BOARD

1. *Does the Board consistently demonstrate, in its own conduct and decisions, the integrity, accountability and respect for rules that it expects from the organisation?*
2. *Are decision-making authority, approval rights and reporting lines clearly allocated between the Board, management, control functions and employees, and documented in a delegation of authority matrix?*
3. *Which key policies has the Board approved, when were they last reviewed, and do they cover the areas that matter most for our risks?*
4. *Does the Board receive timely and reliable information on risks, incidents, control weaknesses and corrective actions, and what happened after the last significant finding?*
5. *Do we know whether our controls are actually followed in practice, and who tests this?*
6. *Is our control environment proportionate to our size and risks, and when did we last review it after a change in the business?*

5.2.2
INTERNAL CONTROL FRAMEWORK

Internal control is a complex and continuous process that includes the selection and application of various internal control measures, thereby increasing the efficiency and effectiveness of the company's activities. Managers and employees at all levels must participate in this process, examining risk factors and providing reasonable assurance that the overall objectives of the organisation are achieved. Internal control is not a single event or circumstance, but a set of actions applied on an everyday basis that cover the activities of the entire organisation.

Internal control is therefore not an addition to the company's activities: it is integrated into the activities of the organisation, rather than added to them.

Importance of internal control

Internal control helps to:

- Avoid surprises
- Assure the adequacy of process performance
- Perform jobs more efficiently and effectively
- Improve the overall quality of the business

There are various standards that define the functioning of internal control in an organisation:

- COSO Internal Control Framework (by COSO)
- ISO 31000 Risk management — Guidelines
- ISO 27001 Information security, cybersecurity and privacy protection — Information security management systems — Requirements
- Global Internal Audit Standards (by IIA)
- COBIT – Control Objectives for Information and Related Technologies (by ISACA)
- Basel Framework (for the banking sector) (by BCBS)

One of the most widely used globally is the COSO Internal Control Framework developed by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).[10] It defines internal control as "a process, effected by an entity's board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives."

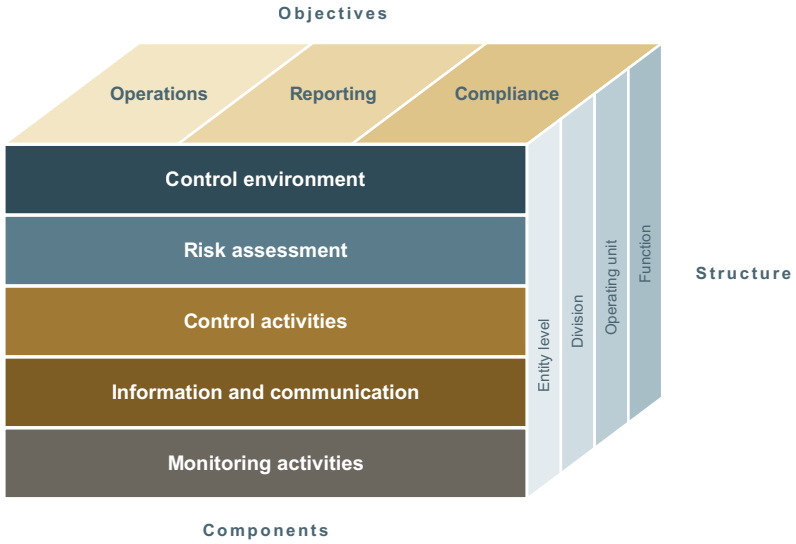
10 Committee of Sponsoring Organizations of the Treadway Commission (COSO), https://www.coso.org/.

Internal control is a process established to provide reasonable assurance regarding the achievement of objectives relating to operations, reporting and compliance. It helps to ensure the reliability of financial reporting, promote operational efficiency, protect assets and ensure adherence to laws and regulations. Beyond compliance, robust internal controls build trust, improve decision-making and contribute to overall integrity and growth.

By applying COSO, a company can obtain many benefits, such as:

- Reduced production downtime and fewer workplace accidents.
- Accurate inventory, reducing financial misstatements.
- Assured compliance with environmental and labour regulations.
- Confidence of the Board and shareholders in reporting and risk management.

Figure 5.1 The COSO Internal Control Framework: the "COSO cube"



Source: BICG, based on COSO (2013), Internal Control – Integrated Framework.

The cube shows the three dimensions of the framework and how they relate: the three categories of objectives (operations, reporting and compliance) on the top face, the five components of internal control on the front face, and the structure of the organisation (entity level, divisions, operating units and functions) on the side. Every component applies to every objective and at every level of the organisation.

Control environment

1. The organisation demonstrates a commitment to integrity and ethical values.
2. The Board of directors demonstrates independence from management and exercises oversight of the development and performance of internal control.

3. Management establishes, with Board oversight, structures, reporting lines, and appropriate authorities and responsibilities in the pursuit of objectives.
4. The organisation demonstrates a commitment to attract, develop, and retain competent individuals in alignment with objectives.
5. The organisation holds individuals accountable for their internal control responsibilities in the pursuit of objectives.

Examples:

- The Board approves a clearly defined code of conduct with which the company must comply, while management implements the code and provides ethics training for employees.
- The Board sets ethical values, for example zero tolerance of bribery in procurement.
- To ensure independence from management, the Board establishes an audit committee and appoints independent Board members to it.
- The Board ensures that the company has a clear and efficient organisational chart and job descriptions, that each role has defined authorities, and that accountability and an efficient flow of information are ensured.
- Management develops and executes rigorous recruitment, training and retention programmes in order to attract employees with the right values and expertise and to train them efficiently.

Risk assessment

6. The organisation specifies objectives with sufficient clarity to enable the identification and assessment of risks relating to objectives.
7. The organisation identifies risks to the achievement of its objectives across the entity and analyses risks as a basis for determining how the risks should be managed.
8. The organisation considers the potential for fraud in assessing risks to the achievement of objectives.
9. The organisation identifies and assesses changes that could significantly affect the system of internal control.

More on risk management can be found in sub-chapter 5.2.3.

Control activities

10. The organisation selects and develops control activities that contribute to the mitigation of risks to the achievement of objectives to acceptable levels.

11. The organisation selects and develops general control activities over technology to support the achievement of objectives.
12. The organisation deploys control activities through policies that establish what is expected and procedures that put policies into action.

Examples:

- Segregation of duties. To prevent fraud, the employee responsible for ordering raw materials is different from the one who receives the materials and from the one who approves the invoice for payment. This ensures that no single person can manipulate the purchasing process for personal gain.
- Safeguarding of data. All company data is backed up daily, with versioning (e.g. versions of the data are kept for the last 90 days).
- Policies and procedures. A food production company could have a “Sanitation and Hygiene Policy” stating that all personnel must maintain a hygienic environment to prevent food contamination.

Information and communication

13. The organisation obtains or generates and uses relevant, quality information to support the functioning of internal control.
14. The organisation internally communicates information, including objectives and responsibilities for internal control, necessary to support the functioning of internal control.
15. The organisation communicates with external parties regarding matters affecting the functioning of internal control.

Examples:

- Financial data. An enterprise resource planning (ERP) system processes all of a company's transactions, from sales to raw material purchases. This system generates reports, like inventory levels or cost of goods sold, which are crucial for management to assess financial performance and ensure the accuracy of financial statements.
- Communicating internally and externally. A whistleblowing hotline through which an employee, supplier or any other person can anonymously report a colleague’s potential fraudulent activity or a safety violation without fear of retaliation.

Monitoring activities

16. The organisation selects, develops, and performs ongoing and/or separate evaluations to ascertain whether the components of internal control are present and functioning.
17. The organisation evaluates and communicates internal control deficiencies in a timely manner to those parties responsible for taking corrective action, including senior management and the Board, as appropriate.

Examples:

- The company's quality assurance system performs automated, real-time checks, immediately flags issues and can even stop the production line.
- Internal audit may audit a specific production process and provide recommendations on what should be improved.

Benefits of using the COSO framework

Instead of developing your own (customised) internal control framework, apply COSO in your organisation. This brings many benefits:

- shareholders, potential investors and other stakeholders will better understand how your internal controls are managed;
- auditing of internal controls will be smoother and more efficient;
- it will be easier for newcomers to understand your internal controls;
- The European Commission describes the COSO Framework as setting "the highest international standards" for internal control. [11]

The Board should lead this framework by establishing a governance structure and providing efficient oversight.

Weak, optimal and excessive internal control

Weak control measures increase the risk of losses and extra costs due to unexpected events in the company.

Optimal application of coordinated control procedures and measures supports successful operations.

Excessive controls create an excessive bureaucratic apparatus, which in itself may hinder the operational effectiveness of the company.

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11 European Commission (2017), Revision of the Internal Control Framework, C(2017) 2373, https://commission.europa.eu/document/download/f163e193-bf9b-4823-bd4b-dceb8739f46e_en.

KEY TAKEAWAYS

A. Internal control is a continuous process, integrated into the company's activities rather than added to them, that provides reasonable assurance on the achievement of objectives relating to operations, reporting and compliance.

B. The COSO Internal Control Framework is the most widely used reference. Its five components are the control environment, risk assessment, control activities, information and communication, and monitoring activities, each with practical principles the Board can use to test the company's system.

C. Applying a recognised framework, rather than a home-made one, makes internal controls easier for shareholders, auditors and newcomers to understand and easier to audit.

D. Controls can be too weak or too strong: weak controls expose the company to losses and surprises, while excessive controls create bureaucracy that hinders operations. The Board should aim for an optimal, coordinated set of controls.

E. The Board leads the framework by establishing the governance structure and providing effective oversight; management designs and operates the controls.

QUESTIONS FOR THE BOARD

1. *Which internal control framework does the company apply, and can management explain how each of the five COSO components is covered?*
2. *Are objectives specified clearly enough for risks to them, including the risk of fraud, to be identified and assessed?*
3. *Are key controls such as segregation of duties, safeguarding of data and written policies in place for the processes that matter most, and are they documented?*
4. *Does the Board receive relevant, quality information on internal control, and are deficiencies reported and corrected in a timely manner?*
5. *Where are our controls too weak, and where are they excessive and slowing the business down?*
6. *How does the Board satisfy itself that the internal control system is present and functioning, and not only described on paper?*

5.2.3

RISK GOVERNANCE, THREE LINES MODEL

The complexity of the business environment and growing uncertainty demand from companies and their Boards a deep understanding of the link between risk and reward in achieving the strategic objectives. Effective risk management enables the Board to pursue the company's strategic objectives with a clear understanding of the risks it is willing to take, reducing surprises and losses, clarifying accountability, strengthening resilience and stakeholder confidence, and revealing opportunities as well as threats.

In the process of risk governance and management it is important to clearly define the roles of the Board, the Board committee responsible for risk oversight, the CEO, the risk officer, management, employees and internal audit.

The Board bears ultimate responsibility for the establishment and oversight of the risk governance system within the company, setting the risk appetite and risk tolerance levels, as well as for making strategic decisions and involving itself in approving or guiding major strategic risks. The Board sets the tone of the risk culture within the company.

The Board risk committee (or any other relevant Board committee involved in risk governance) is a corporate body that **assists** the Board in performing risk oversight by monitoring the risk management processes in greater depth, conducting regular reviews of the effectiveness of the company’s risk management processes, evaluating the identification, assessment and mitigation of risks, participating in the development and review of risk management policies and procedures, providing guidance and recommendations to the Board on risk-related decisions, and remaining accountable to the Board.

The Chief Executive Officer (CEO) has ultimate responsibility for the overall success of the risk management process at the operational, day-to-day level. The CEO ensures the effectiveness of risk management and emphasises its importance throughout the organisation.

The Chief Risk Officer (CRO) coordinates and supports the risk management process within the company. The CRO helps to identify and assess risks across the various aspects of the business, develops and helps to implement strategies to

mitigate identified risks, and reports regularly to the CEO, the relevant Board committee and the Board on the status of risks and risk management efforts.

Employees should be aware of, understand and manage the risks associated with their roles and the functions for which they are responsible. They are expected to report potential risks or issues to their supervisors and the Chief Risk Officer.

Internal audit is responsible for the independent evaluation of the quality and effectiveness of the risk management system as a whole. Internal audit is accountable not to the CEO but directly to the Board, and provides reports, insights and recommendations directly to the Board and the relevant Board committee.

Risk appetite

- Risk appetite is the amount of risk an entity is willing to accept in pursuit of value.
- Risk appetite is directly related to the entity's strategy. It is considered in strategy-setting, where the desired return from a strategy should be aligned with the entity's risk appetite. Different strategies expose the entity to different risks.
- The entity's risk appetite guides resource allocation. Management allocates resources across business units with consideration of the entity's risk appetite and each business unit's strategy for generating the desired return on invested resources.

Risk tolerance

- Risk tolerances are the **acceptable levels of variation relative to the achievement of objectives**.
- Risk tolerances can be measured, and are often best measured in the same units as the related objectives. Performance measures are aligned to help ensure that actual results remain within the acceptable risk tolerances.
- In setting risk tolerances, management considers the relative importance of the related objectives and aligns the risk tolerances with the risk appetite.

The four steps of risk management

Risk management is a continuous cycle that the company repeats as its business and environment change: identify the risks, evaluate them, decide how to respond and monitor the result. Management runs the cycle; the Board sets its direction and oversees it. Good practice starts with a clear statement of risk appetite, approved by the Board, which defines how much risk the company is willing to take in pursuit

of its objectives and gives each of the four steps a common reference point. A Board that understands the cycle well is able to judge whether management performs each step properly, to ask the right questions at each stage and to recognise the moments when its own decision is required. There are four key steps in the risk cycle.

Step 1. Identify

The first step is to establish what could prevent the company from achieving its objectives, and what opportunities it might be missing. This is done by management, ideally with the involvement of people from across the business, since the risks that matter most are often visible only to those closest to operations, customers or technology. Sources include strategic reviews, workshops, incident and near-miss records, audit findings, external reports and scenario analysis. The output is a risk register: a living list in which each risk has a description, a category (strategic, financial, operational, compliance, reputational, technology, sustainability) and a named owner. For the Board, the practical questions are whether the register is complete rather than long, whether it looks forward as well as backward, and whether emerging risks such as cyber threats, regulatory change, climate transition or a concentration of key suppliers or customers have been considered. A register that has not changed in two years is a warning sign in itself.

In practice, risk owners often find it difficult to identify the risks in the processes for which they are responsible. To help with this initial task, see Annex 3, Risk categories and types.

Step 2. Evaluate

Each identified risk is then assessed by its likelihood and its potential impact, taking into account the controls that already exist. The result is usually expressed on a simple scale and plotted on a likelihood–impact matrix, which allows the company to distinguish the few risks that require Board attention from the many that management handles in the ordinary course of business. Evaluation should consider the inherent risk (before controls) and the residual risk (after controls), because the gap between the two shows how much the company depends on its controls working. It should also consider velocity, that is how quickly a risk could materialise, and the possibility of several risks occurring together. The Board should expect the evaluation to be honest rather than comfortable, should challenge scores that seem too optimistic or too high (a useful check is to compare how similar risks have been scored by different units) and should ask how the residual risk compares with the risk appetite and tolerances it has set.

Step 3. Respond

For each significant risk the company chooses a response: avoid the risk by stopping or not starting the activity that creates it; reduce it through controls, procedures and training; transfer all or part of it to a third party through insurance, contract, outsourcing or hedging; or accept it knowingly and keep it under watch. The choice is guided by the risk appetite and by the cost of the response compared with its benefit. Some responses require the Board's own decision, for example withdrawing from a market, changing the capital structure or entering into a major insurance or hedging programme, while most are decided by management within the limits the Board has set. Whatever the choice, it should be recorded in the risk register with the responsible owner, the actions to be taken and the deadline. The most common failure at this step is a response that exists on paper only; the Board should ask not only what the response is but whether it has actually been implemented. Risks may also present opportunities, and a good response considers whether the company could take more of a well-understood risk rather than less.

Step 4. Monitor

The final step keeps the cycle alive. Management tracks the risks through key risk indicators, reviews the register at least quarterly and reports material changes, incidents and near misses to the Board or its risk or audit committee. Internal audit, as the third line, independently tests whether the controls and responses work as intended, and the external auditor and other assurance providers add their own perspective. Monitoring is also where learning happens: every incident should be followed by a short review of what the risk register said before it happened and what needs to change. The Board's role is to receive reporting that is timely and integrated rather than fragmented, to see that the actions agreed at step 3 are completed, and to review at least once a year whether the risk management system as a whole, including the risk appetite, still fits the company's strategy, size and environment. It is good practice for the Board to review the principal risks and the progress of the risk responses each quarter, while the risk or audit committee conducts the deeper analysis. The recommended elements of a risk register are listed in Annex 4.

What the Board should do

In practice the Board's involvement in the cycle comes down to a few recurring actions: set and periodically revisit the risk appetite and tolerances; approve the risk management policy and the allocation of roles under the Three Lines Model; review the principal risks and their responses at least once a year and the risk register more often through a committee; take the decisions that are reserved for it; and

obtain independent assurance that the cycle operates in reality and not only in the documents. A Board that does these things consistently will rarely be surprised, and when it is, it will be in a position to respond quickly.

Figure 5.2 **Risk matrix: evaluating risks by likelihood and impact**



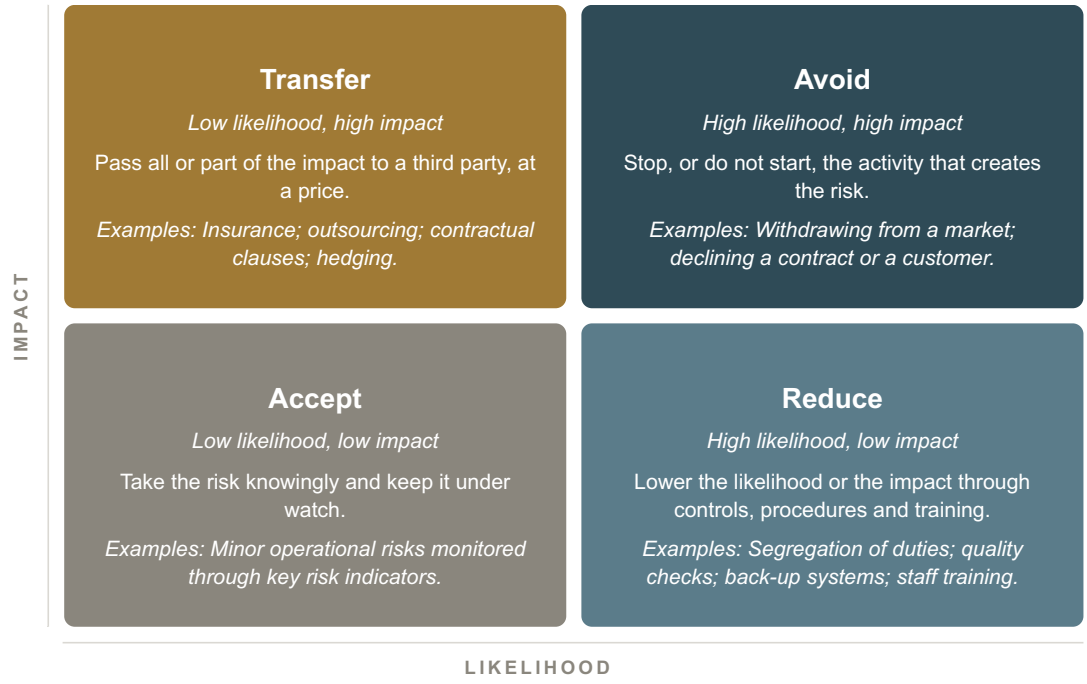
Score = likelihood (1–5) × impact (1–5). The scales, thresholds and colours should be adapted to the company's size and risk appetite.

The risk matrix is the most common tool for the second step of the risk management cycle. Each risk is scored for likelihood and for impact on a scale of one to five, and the product of the two places it in one of four levels. Risks in the low band are accepted and monitored; risks in the medium band are managed through controls and reported by their owners; risks in the high band require an action plan and the attention of the risk or audit committee or the Board; and risks in the extreme band are outside the risk appetite and call for immediate action and a Board decision. The matrix should be applied to the residual risk, after existing controls, and the scales, thresholds and colours should be defined in the company's risk management policy and adapted to its size and risk appetite.

Four strategies for risk response

Once a risk is assessed by likelihood and impact, the company chooses one of four responses: avoid, reduce, transfer or accept. The choice should reflect the Board-approved risk appetite and the cost-benefit of the response. Each response should be recorded in the risk register, assigned to a risk owner and monitored through appropriate indicators and assurance activities.

Figure 5.3 **Four strategies for risk response by likelihood and impact**



Avoiding a risk means eliminating the threat entirely by choosing not to engage in the activity that carries the risk. For instance, a company may decide not to expand into a new country with an unstable political climate, to avoid the risk of asset seizure or business disruption.

Transferring a risk means shifting the financial and/or operational burden of a risk to a third party, for example by purchasing an insurance policy or outsourcing the company's IT services to a specialised firm, thereby transferring the technical risks associated with network security and maintenance to the third-party provider.

Reducing, or mitigating, a risk involves taking steps to lower the probability or the impact of a risk. This is the most common strategy and is used when a risk cannot be avoided completely but its effects can be managed. A construction company might reduce the risk of on-site injuries by enforcing strict safety protocols and providing personal protective equipment; to reduce the risk of a data breach, a company might invest in stronger cybersecurity software, implement multi-factor authentication and provide mandatory training for all employees on phishing.

Accepting a risk involves making a conscious decision to take no action to reduce or transfer the risk, and simply to absorb the consequences if it occurs. This is typically done for risks with low probability and low impact, where the cost of a response would be greater than the potential damage. A company might accept the minor risk of currency fluctuations when doing a small amount of business abroad, as the cost of hedging would outweigh the potential losses. Similarly, a project

manager might accept the risk of a minor, non-critical task running a day late, knowing that it will not affect the project's overall deadline.

Risk management frameworks

There are several risk management frameworks. The most widely used are the COSO Enterprise Risk Management – Integrating with Strategy and Performance and the ISO 31000 standard.

ISO 31000 is an international standard recognised globally. It provides a common language for risk management, making it easier for companies operating in different countries or industries to communicate about risk. The standard is known for its flexibility: it provides principles and guidelines rather than specific requirements, allowing organisations to adapt the framework to their specific needs and contexts. [12]

COSO provides a comprehensive framework that covers internal control, enterprise risk management and fraud deterrence. It is well established and widely used. It integrates risk management with internal control, which can be beneficial for companies looking to align risk management with broader governance and control activities. The framework focuses on aligning risk management with the achievement of organisational objectives, helping organisations to better understand and manage the risks that might affect their goals.

The suitability of a particular framework depends on the organisation's needs, industry and preferences.

Enterprise risk management: the culture, capabilities, and practices integrated with strategy-setting and performance, that organizations rely on to manage risk in creating, preserving and realizing value. [13]

12 ISO 31000:2018, Risk management – Guidelines. Introductory materials: https://practicalrisktraining.com/iso31000; https://pecb.com/whitepaper/iso-31000-risk-management--principles-and-guidelines.
13 COSO (2017), Enterprise Risk Management – Integrating with Strategy and Performance, https://www.coso.org/pages/erm-integratedframework.aspx.

Figure 5.4 **COSO Enterprise Risk Management framework: five components and twenty principles**



Source: adapted from the Committee of Sponsoring Organizations of the Treadway Commission (COSO), Enterprise Risk Management – Integrating with Strategy and Performance, 2017.

Three Lines Model

The Three Lines Model (known until 2020 as the Three Lines of Defence Model, and refreshed in July 2026) is a governance and risk management framework developed by the Institute of Internal Auditors (IIA). It provides clarity on roles and responsibilities in risk management, assurance, and oversight. Additionally, it ensures that value creation, risk-taking, and accountability are aligned across the organisation.[14]

While the COSO Framework explains and helps to design and evaluate effective internal control processes, the Three Lines Model explains who does what in governance, risk, control and assurance, and ensures clear roles and accountability.

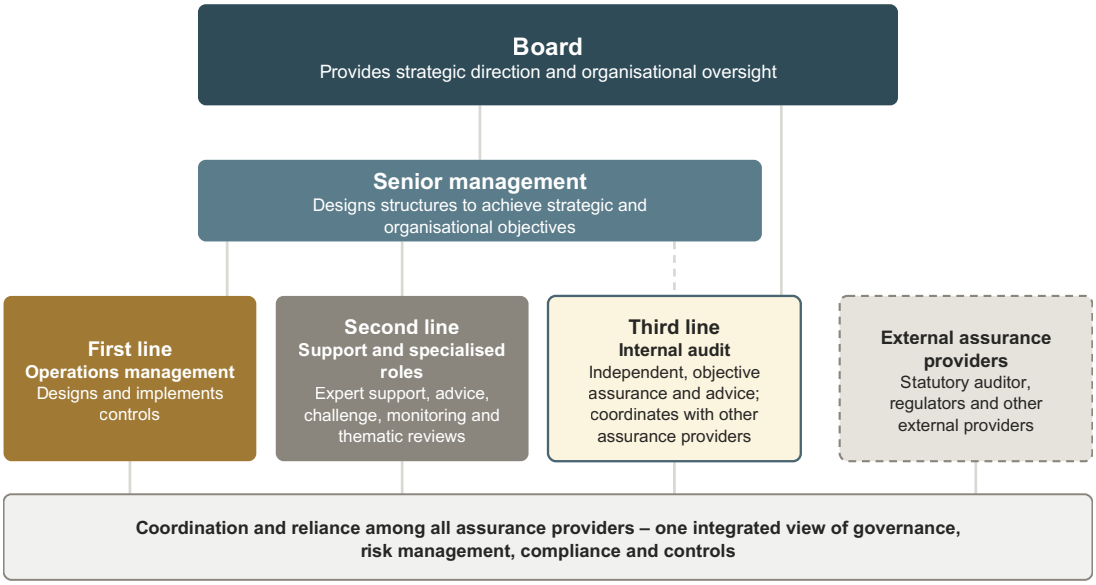
Benefits of implementing the Three Lines Model in a company:

- Clarifies roles, responsibilities and accountability – prevents gaps and overlaps in risk management.
- Strengthens governance – supports the Board's oversight role.
- Enhances resilience – enables early risk detection and effective response.
- Improves assurance – ensures that the Board receives reliable, objective information.

14 The Institute of Internal Auditors, www.theiia.org.

– Meets stakeholder expectations – regulators, investors and rating agencies increasingly expect structured governance models.

Figure 5.5 The Three Lines Model (The IIA, refreshed in July 2026)



Solid line: functional reporting and oversight Dashed line: administrative reporting Dashed border: outside the organisation

Source: adapted from The Institute of Internal Auditors, Assurance and Advice in Support of Effective Governance: Three Lines Model, Statement of Position, 2026.

Each of the three lines ***plays a distinct role*** in the company's control environment:

1. The first line (functions that own and manage risks)
   This line is formed by the managers and staff who are responsible for identifying and managing risk as part of their accountability for achieving objectives. Collectively, they should have the necessary knowledge, skills, information and authority to operate the relevant risk control policies and procedures. This requires an understanding of the company, its objectives, the environment in which it operates and the risks it faces. These are the operational teams directly involved in delivering products or services; they own and manage the risks related to their daily activities.

2. The second line (functions that oversee, or specialise in, compliance or the management of risk)

   These are the specialists in areas such as risk management, compliance, quality control or finance, who monitor and oversee the first line's risk management activities, ensure adherence to policies and regulations, and help the first line to set up the right tools and processes for managing risk.

The second line provides the policies, frameworks, tools, techniques and support that enable risk and compliance to be managed in the first line, conducts monitoring to judge how effectively this is done, and helps to ensure consistency in the definition and measurement of risk.

3. The third line (functions that provide independent assurance)
   This is provided by internal audit. Sitting outside the risk management processes of the first two lines, its main roles are to ensure that the first two lines are operating effectively and to advise how they could be improved. Tasked by, and reporting to, the Board or audit committee, it provides a risk-based evaluation of the effectiveness of governance, risk management and internal control to the organisation's governing body and senior management. It can also give assurance to sector regulators and external auditors that appropriate controls and processes are in place and operating effectively.

The structure of the **model refreshed in 2026** is unchanged, but the emphasis has shifted. **Assurance and advice are now treated as distinct but complementary**: assurance confirms whether processes are adequate and effective, and is credible only where the provider neither designs nor operates the process, while advice identifies improvements and emerging issues and allows closer collaboration with management. The **refreshed model calls for coordination and reliance among all assurance providers**, internal and external, to reduce overlap and "assurance fatigue", and **names internal audit as the integrator** that **gives the Board one system-wide view** of how governance, risk management, compliance and controls work together. **Independence is defined more precisely**, through functional reporting to the Board, autonomy over scope, unrestricted access to information, adequate resources and protection from retaliation, but "should not be interpreted as isolation". Finally, the model accepts that roles in real companies are often blended and **sets out safeguards for such cases, such as Board approval, clear separation of activities, full disclosure and periodic independent review**, while confirming that outsourcing an activity change neither its place in the model nor the Board's accountability.[15]

Recommendations for the Board

1. ***Set the tone***: endorse and actively support the use of the Three Lines Model.
2. ***Demand clarity***: request clear definitions of roles, responsibilities and accountabilities across the lines.
3. ***Monitor balance***: ensure no line becomes too dominant or too weak.

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15 The IIA (2026), Assurance and Advice in Support of Effective Governance: Three Lines Model, Statement of Position.

4. ***Ensure the independence of internal audit***: its reporting line should go directly to the audit committee or the Board.
5. ***Promote collaboration***: encourage open communication among all three lines to prevent duplication or blind spots.
6. ***Request integrated assurance reporting***: ensure that the Board receives a consolidated view of risks, controls and assurance.
7. ***Review effectiveness regularly***: include the effectiveness of the model in governance reviews.
8. ***Stay informed***: request regular training or updates on governance, risk and assurance frameworks.

The most common mistakes in implementing the Three Lines Model:

- Lack of tone at the top from the Board.
- Treating it as a rigid checklist instead of a flexible model adapted to the organisation's needs.
- Blurred role boundaries – e.g. management expecting internal audit to design controls, or risk and compliance functions acting as internal auditors.
- Poor communication between lines – leading to duplicated or missed assurance.
- Underestimating the Board's role – some Boards assume the model is only for management, but the governance tone must come from the top.
- Overloading the third line with both advisory and assurance duties, undermining independence.

More information on this model is available on the IIA website.[16]

KEY TAKEAWAYS

A. The Board bears ultimate responsibility for the risk governance system: it sets the risk appetite and risk tolerances, approves or guides major strategic risks and sets the tone of the risk culture. A risk committee, where established, prepares this work but remains accountable to the Board.

B. Roles must be clear: the CEO is responsible for risk management at the operational level, the Chief Risk Officer coordinates and reports, employees manage the risks of their own roles, and internal audit independently evaluates the whole system and reports directly to the Board.

C. Risk management follows four steps: identify the risks, evaluate them by likelihood, impact and control effectiveness, select a response (avoid, transfer, reduce or accept) and monitor through a risk register, key risk indicators and audits.

D. Risk appetite is the amount of risk the company is willing to accept in pursuit of value; risk tolerances are the acceptable variations around objectives. Both should be set with the strategy and guide resource allocation. Risks may also present opportunities.

E. The Three Lines Model clarifies who does what: the first line owns and manages risk, the second line provides expertise, oversight and monitoring, and the third line (internal audit) provides independent assurance to the Board. Its most common failures are a lack of tone at the top, blurred role boundaries and poor communication between the lines.

QUESTIONS FOR THE BOARD

1. *Has the Board set the company's risk appetite and risk tolerances, and are they linked to the strategy and used in resource allocation?*
2. *Are the roles of the Board, its risk committee, the CEO, the risk officer, employees and internal audit in risk governance clearly defined and understood?*
3. *Do we maintain a current risk register with risk owners, key risk indicators and mitigation measures, and when did the Board last review it?*
4. *For our most significant risks, has the Board consciously chosen a response (avoid, transfer, reduce or accept) rather than accepting them by default?*
5. *Do the three lines in our company work as intended: does the first line own its risks, does the second line have the authority to challenge it, and does internal audit report directly to the Board?*
6. *Does the Board receive an integrated view of risks, controls and assurance, and is the effectiveness of the risk governance system itself reviewed regularly?*

16 The Institute of Internal Auditors, www.theiia.org.

5.2.4

RESILIENCE: CRISIS PREPAREDNESS, BUSINESS CONTINUITY AND RECOVERY

Why resilience matters

Corporate resilience is the ability of a company to anticipate, prepare for, respond to and recover from significant disruptions while protecting its people, assets, operations, reputation and long-term value. Resilience is not limited to emergency response. It includes crisis preparedness, business continuity, disaster recovery, communication with stakeholders, and the ability to learn and adapt after disruption.

The importance of resilience has increased significantly in recent years due to geopolitical instability, cyber threats, pandemics, supply chain disruption, climate-related events, energy insecurity, regulatory change and social expectations. The G20/OECD Principles of Corporate Governance expressly include a chapter on **Sustainability and resilience**, and emphasise that Boards should consider material sustainability risks and opportunities when reviewing strategy, risk management and internal control systems.

For the Board, resilience is not an operational detail to be left entirely to management. It is part of the Board's responsibility for strategic guidance, effective monitoring of management, risk oversight and accountability to the company and its shareholders.

In the European Union, resilience's importance is increasing as a legal requirement as well as good practice. The NIS2 Directive on cybersecurity, the Digital Operational Resilience Act (DORA) for the financial sector and the Critical Entities Resilience Directive, as transposed in Estonia, Latvia and Lithuania, require many companies to manage their risks, maintain business continuity and report significant incidents, and in several cases place explicit responsibility on the management body. The Board should know which of these regimes apply to the company and how compliance is assured.[17]

What corporate resilience includes

Corporate resilience should be understood as an integrated governance framework and as a legal duty of the companies and their Boards covering four connected

17 Directive (EU) 2022/2555 on measures for a high common level of cybersecurity (NIS2); Regulation (EU) 2022/2554 on digital operational resilience for the financial sector (DORA); Directive (EU) 2022/2557 on the resilience of critical entities (CER).

areas, supported by crisis communication and by learning from every incident, both of which are addressed below:

Crisis preparedness means the company's readiness to identify, assess and prepare for serious events that may threaten its operations, people, financial position, licence to operate or reputation.

Emergency response means the immediate actions taken when an incident occurs, including protection of life and health, mitigation of damage, activation of crisis teams, internal escalation and communication with relevant authorities and stakeholders.

Business continuity means the ability of the company to continue its most critical activities at an acceptable level during disruption. A business continuity plan identifies critical functions, key dependencies, minimum service levels, alternative processes, responsibilities and recovery priorities.

Disaster recovery usually refers to the restoration of critical systems, infrastructure, data and technology after a disruption. It is particularly relevant for IT, cybersecurity, data protection, operational technology and other infrastructure on which business continuity depends.

These areas should not be managed as separate documents without coordination. A company may have a crisis management plan, business continuity plan, disaster recovery plan, cyber incident response plan, communication plan and other related documents, but they should form one coherent resilience framework. The Board should be able to understand how these documents fit together, who owns them, when they are activated, and how they are tested.

The Board's role in resilience

The Board is not expected to manage an emergency on a day-to-day basis. Operational responsibility normally belongs to the CEO and management. However, the Board should ensure that the company has an appropriate resilience framework, that management is prepared for serious disruptions, and that the company can continue to protect long-term value under stress.

The Board should approve the company's overall approach to resilience, including the risk appetite, governance structure, reporting arrangements and escalation criteria. It should satisfy itself that resilience is embedded in strategy, risk management, internal control, compliance, sustainability and capital allocation.

The Board should also ensure that the company has identified its most material disruption scenarios. These may include cyberattacks, loss of key systems, loss of premises, supply chain failure, energy disruption, industrial accidents, fraud, regulatory intervention, sanctions exposure, pandemics, extreme weather events, product safety incidents, liquidity shocks, reputational crises or loss of key people.

A mature Board should not only ask whether plans exist. It should ask whether they are realistic, tested, understood by the right people, supported by adequate resources, and capable of being executed under pressure.

Responsibilities of management

Management is responsible for designing, implementing and maintaining the company's resilience arrangements. This includes preparing relevant plans, assigning roles, training employees, maintaining emergency contacts, ensuring data back-up and system recovery, engaging with critical suppliers, organising simulations and reporting material weaknesses to the Board.

Management should ensure that the company has clear procedures for incident detection, escalation, decision-making and communication. In a crisis, delays, uncertainty and unclear authority may cause as much damage as the incident itself. Therefore, the company should know in advance who has authority to activate the crisis plan, who leads the crisis team, who communicates with employees, regulators, customers, shareholders and media, and when the Board must be informed or convened.

Management should also maintain an up-to-date view of critical dependencies. These include key people, key suppliers, technology systems, outsourced service providers, premises, logistics, licences, funding arrangements, insurance cover and regulatory permissions.

Crisis management and emergency response

A crisis may develop rapidly and under conditions of uncertainty. The purpose of crisis management arrangements is to ensure that the company can make timely, coordinated and well-informed decisions when normal management processes are insufficient.

A crisis management plan should define:

AREA	KEY QUESTION
1. **Activation**	What events trigger the crisis plan?
2. **Escalation**	When must the CEO, Chair, Board or committee be informed?

AREA	KEY QUESTION
3. **Crisis team**	Who is responsible for leading the response?
4. **Decision authority**	Who can make urgent decisions?
5. **Stakeholder communication**	Who communicates with whom, and through which channels?
6. **Regulatory obligations**	Which notifications may be required?
7. **Documentation**	How are decisions and actions recorded?
8. **Recovery**	How does the company return to normal operations?
9. **Learning**	How are lessons identified and implemented?

The Board should agree in advance which events require immediate notification to the Chair, the full Board or a relevant Board committee. For example, the Board should normally be informed promptly of incidents that may have a material impact on people's safety, financial stability, legal compliance, market disclosure, reputation, business continuity, data security or licence to operate.

Business continuity plan

A business continuity plan should identify how the company will continue its essential operations during a disruption. It should be practical, proportionate and tailored to the company's size, sector, complexity and risk profile.

At a minimum, the business continuity plan should address:

AREA	MATTERS TO BE COVERED
1. **Critical functions**	Which activities must continue during disruption
2. **Recovery priorities**	Which services, processes or sites must be restored first
3. **Minimum acceptable level of service**	What level of operation is acceptable during disruption
4. **Roles and responsibilities**	Who activates and manages the plan
5. **Key dependencies**	People, systems, suppliers, premises, data and funding
6. **Alternative arrangements**	Remote work, substitute suppliers, alternative sites, manual processes
7. **Communication**	Employees, customers, regulators, shareholders, suppliers and media

AREA	MATTERS TO BE COVERED
8. **Testing**	Exercises, simulations and lessons learned
9. **Review cycle**	Regular updates and approval process

The business continuity plan should not be a formal document prepared only for compliance purposes. It should be capable of being used in real time. The Board should therefore receive assurance that the plan is up-to-date, tested and known by the relevant people.

Disaster recovery plan

A disaster recovery plan should set out how the company will restore critical systems, data, infrastructure and technology following a major disruption. For many companies, disaster recovery is closely linked to cybersecurity, data protection, digital operations, customer service and financial reporting.

The disaster recovery plan should define recovery time objectives and recovery point objectives (RTO and RPO) for critical systems. In simple terms, the company should know how quickly each critical system must be restored and how much data loss, if any, is acceptable. The plan should also address back-up arrangements, access rights, third-party service providers, cloud infrastructure, alternative communication channels and manual workarounds.

The Board does not need to review every technical detail. However, it should understand whether recovery assumptions are realistic, whether critical systems have been tested, whether there are single points of failure, and whether the company has adequate cyber and technology resilience.

Crisis communication

Communication is a central part of resilience. In a crisis, unclear or inconsistent communication can damage trust, increase legal risk and undermine the company’s reputation. The company should have prepared communication protocols for employees, customers, regulators, shareholders, creditors, suppliers, communities, media and other relevant stakeholders.

The Board should ensure that the company’s communication approach is accurate, timely, responsible and aligned with legal obligations. For listed companies, crisis communication may also involve market disclosure obligations. For regulated companies, communication with supervisory authorities may be critical. For companies providing essential services, communication with customers, municipalities, government bodies and the public may be equally important.

The company should avoid both excessive silence and premature speculation. Good crisis communication should explain what is known, what is being done, what stakeholders should do, and when further information can be expected.

The Board should ensure that the company has a written crisis communication plan that is approved at the appropriate management level and reviewed by the Board or relevant Board committee. The plan should be proportionate to the company's size, sector, ownership structure, regulatory status and risk profile.

Testing and Board assurance

Resilience cannot be assessed only by the existence of written plans. Plans should be tested through exercises, simulations, scenario discussions and post-incident reviews. Testing helps to reveal gaps in decision-making, communication, technology recovery, supplier readiness, employee awareness and Board escalation.

The Board should receive periodic assurance on resilience. This may include management reports, internal audit reviews, external assessments, cyber resilience testing, supplier resilience reviews, insurance reviews and tabletop exercises involving senior management and, where appropriate, Board members.

A useful practice is to conduct at least one annual Board-level resilience discussion. This may focus on a major scenario such as cyberattack, loss of a critical supplier, liquidity stress, geopolitical disruption, energy shortage, product safety incident or reputational crisis. The purpose is not to predict the future precisely, but to test whether the company can think and act under pressure.

Good governance practices

A company with a sound resilience framework will usually have the following features:

GOOD PRACTICE	EXPLANATION
Board-level oversight	The Board periodically reviews resilience risks, plans and test results
Clear management ownership	A senior executive is responsible for resilience coordination
Integrated plans	Crisis management, business continuity and disaster recovery plans are aligned
Defined escalation	The company knows when and how to inform the CEO, Chair and Board
Tested procedures	Plans are tested through realistic exercises

GOOD PRACTICE	EXPLANATION
Critical dependency mapping	Key systems, people, suppliers and sites are identified
Communication protocols	Internal and external communication responsibilities are clear
Supplier resilience	Critical third-party dependencies are reviewed
Cyber resilience	Technology recovery and cyber response are regularly tested
Lessons learned	Incidents and exercises lead to documented improvements
Regular reporting	The Board receives concise, decision-useful information
Proportionality	Arrangements reflect the company's size, sector and complexity

KEY TAKEAWAYS

A. Corporate resilience is the ability to anticipate, prepare for, respond to and recover from serious disruption while protecting people, assets, operations, reputation and long-term value. It is part of the Board's responsibility for strategy, risk oversight and accountability, not an operational detail.

B. Resilience is one integrated framework: crisis preparedness, emergency response, business continuity and disaster recovery, supported by crisis communication and learning from incidents. The Board should know how the plans fit together, who owns them, when they are activated and how they are tested and results assessed.

C. The Board does not manage emergencies, but it approves the overall approach and risk appetite, ensures that the most material disruption scenarios and critical dependencies have been identified, and agrees in advance which events must be escalated to the Chair, the Board or a committee.

D. For many companies' resilience is also a legal duty under EU rules such as NIS2, DORA and the Critical Entities Resilience Directive, with obligations on the management body.

E. Plans are only as good as their testing. The Board should receive periodic assurance on resilience and hold at least one Board-level resilience discussion a year around a major scenario.

F. Good crisis communication is prepared in advance for all key stakeholders, avoids both silence and speculation, and is aligned with disclosure and regulatory obligations.

QUESTIONS FOR THE BOARD

1. *What are the most serious disruption scenarios that could affect the company, and which activities, systems, people and suppliers are critical to continuing operations?*
2. *Do we have approved and tested crisis management, business continuity and disaster recovery plans, and do they form one coherent framework with clear ownership?*
3. *Who has the authority to activate the crisis plan, and when must the Chair, the Board or a Board committee be informed?*
4. *Which resilience-related legal regimes (NIS2, DORA, critical entities) apply to us, and how is compliance assured?*
5. *Have we tested crisis decision-making at senior management and Board level, and what did the last exercise, incident or near miss teach us?*
6. *Are our communication protocols clear for employees, regulators, shareholders, customers and the media, and consistent with our disclosure obligations?*
7. *Do we understand our critical third-party and outsourced dependencies, and is our insurance cover, including D&O, cyber and business interruption, adequate?*
8. *Does internal audit or another assurance provider review our resilience arrangements, and are resilience risks reflected in strategy, capital allocation and risk appetite?*
9. *In a group, are the group resilience policies suitable for each subsidiary, and could we continue critical operations if several disruptions occurred at the same time?*

5.2.5

CYBERSECURITY AND INFORMATION SECURITY OVERSIGHT

Cybersecurity oversight

With increased reliance on digital technologies, cybersecurity has become a significant concern. The Board is responsible for overseeing the company's cybersecurity measures, ensuring the protection of sensitive data and mitigating potential risks.

The key areas of its responsibility are:

1. ***Strategic oversight:*** integrate cybersecurity risks into the overall company strategy and ensure an understanding of how cyber threats could affect the business goals and financial performance of the entire organisation.
2. ***Oversight and accountability:***
    a. Be aware of and understand the key cyber risks. The Board should be informed about the most significant cyber risks the company faces and how management is addressing them.
    b. Monitor cyber resilience: oversee the company's ability to withstand and recover from cyberattacks.
3. ***Board expertise:*** the Board and its designated committee (if any) should have clear ownership of cybersecurity oversight. Board members may seek additional training, if needed, to fulfil this responsibility professionally and effectively.

By actively engaging in these areas, the Board can help the company to mitigate cyber risks and protect its critical assets, ensuring its resilience.

More on cybersecurity oversight can be found in "Cyber-Risk Oversight – Key Principles and Practical Guidance for Corporate Boards in Europe".[18]

Information security oversight

Information security is one of the core elements of corporate resilience, risk management and internal control. It covers the protection of the company's information, systems, data, networks, digital assets and critical technology infrastructure against unauthorised access, misuse, loss, disruption, manipulation or disclosure. It is directly linked to strategy, business continuity, legal compliance,

18 BICG (2020), Cyber-Risk Oversight – Key Principles and Practical Guidance for Corporate Boards in Europe, https://www.bicg.eu/wp-content/uploads/2020/09/Handbook-1.pdf.

customer trust, reputation, financial reporting, personal data protection, intellectual property and long-term value creation. It also supports operational resilience, strategic decision-making and the company's ability to maintain critical services during disruption.

The Board should ensure that the company has a clear information security policy, defined roles and responsibilities, and regular reporting to the Board and/or a relevant Board committee. Management should be able to explain which information assets and systems are critical, what the main threats are, what controls are in place, how incidents are detected and escalated, and how the company would respond to and recover from a serious cyber or information security incident.

Information security oversight should cover at least the following areas:

AREA	WHAT THE BOARD SHOULD ENSURE
Governance	Clear accountability for information security at executive level
Risk appetite	Agreed level of acceptable information security and cyber risk
Critical assets	Identification of critical data, systems, infrastructure, intellectual property, artificial intelligence systems and operational technology
Controls	Appropriate preventive, detective and corrective controls
Incident and crisis response	Tested procedures for detecting, escalating, responding to and recovering from incidents, including communication, authorities' notification and stakeholder coordination arrangements
Business continuity	Alignment between information security, business continuity and disaster recovery plans
Third parties	Oversight of information security risks from suppliers, cloud providers, outsourced services, software dependencies, supply chains and group companies
People	Employee awareness, access controls, training, insider-risk management and information security culture
Legal compliance	Compliance with data protection, cyber, sectoral and disclosure obligations
Assurance	Internal audit, external testing, penetration testing or independent reviews where appropriate
Reporting	Clear, concise and decision-useful reporting to the Board

The Board should receive regular information security reporting. Such reporting should not be limited to technical metrics. It should help the Board understand whether the company is operating within its risk appetite and whether management

is improving the company's resilience. Useful Board-level indicators may include material incidents and near misses, results of cyber exercises, status of critical remediation actions, employee training completion, phishing and social engineering test trends, vulnerability remediation, third-party risk exposure, audit findings, disaster recovery test results, insurance coverage and regulatory developments.

The Board should also ensure that the company periodically tests its information security arrangements. This may include tabletop exercises, cyber incident simulations, disaster recovery tests, penetration testing, supplier-risk reviews and crisis communication exercises. Lessons learned should be reported to the Board, with clear owners and deadlines for improvement actions.

The Board also plays an important role in setting the tone for security culture across the organisation. Information security should be treated as a shared business responsibility rather than solely a technical or IT matter.

Information security risks increasingly arise through third parties, outsourced services, software providers and interconnected supply chains. The Board should ensure that supplier risk management is proportionate to the company's critical services, dependencies and regulatory obligations, particularly where critical operations, data or technology services rely on external providers.

In company group structures, information security policies may be developed at group level. However, the Board of each subsidiary should consider whether group policies are suitable for the subsidiary's own business, systems, regulatory environment, risk profile and stakeholder interests. Group consistency is valuable, but it should not replace the subsidiary Board's responsibility to ensure that the subsidiary has adequate information security governance and resilience.

Effective Board oversight does not require technical expertise from every Board member, but it does require sufficient understanding to ask informed questions, challenge management and support informed decision-making.

The key expectation is that the Board should **oversee, challenge and assure**, not manage technical details. A robust information security framework should give the Board confidence that management understands the company's digital risks, has implemented proportionate controls, can respond effectively to incidents, manages critical dependencies and continuously improves the company's resilience and security culture.

KEY TAKEAWAYS

A. Cybersecurity and information security are strategic risk governance matters, not IT matters. The Board oversees, challenges and assures; it does not manage the technical detail, but it must understand enough to ask informed questions.

B. The Board should ensure that there is a clear information security policy, executive-level accountability, an agreed risk appetite for cyber and information risk, identified critical assets, proportionate controls and tested incident, continuity and recovery procedures.

C. Board reporting should go beyond technical metrics: material incidents and near misses, exercise results, remediation status, training and phishing test trends, third-party exposure, audit findings and regulatory developments.

D. Information security risks increasingly come through suppliers, cloud providers, software dependencies and group companies; supplier risk management must be proportionate to the company's critical dependencies.

E. In a group, each subsidiary Board remains responsible for ensuring that group policies are suitable for its own business and risk profile. The Board also sets the tone for a security culture in which information security is a shared business responsibility.

QUESTIONS FOR THE BOARD

1. *What are our most critical information assets, systems and data, and who is accountable for their security at executive level?*
2. *Is cyber and information security risk included in the company's risk appetite and risk register, and integrated into the strategy?*
3. *Which third-party, cloud and software dependencies could significantly disrupt our critical operations, and how are they overseen?*
4. *Do we understand the risks associated with emerging technologies, including artificial intelligence and automation?*
5. *How often does the Board receive information security reporting, and what were the most significant incidents, near misses or control weaknesses in the last year?*
6. *Have our incident response, business continuity and disaster recovery plans been tested, and were the lessons translated into concrete improvements?*
7. *Do we have sufficient internal expertise and independent external assurance, and are employees and managers properly trained?*
8. *Does the Board itself have sufficient understanding to challenge management on cyber risk, or should it seek training or expert support?*

5.2.6

INTERNAL AND EXTERNAL AUDIT

The Board (with the support of the audit committee) is responsible for the proper oversight of the company's control system. In this regard, the best friends of the Board and the audit committee are a well-functioning internal audit function and an independent, professional external auditor.

Responsibility for the development and operation of sound risk management and internal control systems lies with management. The Board (with the support of the audit committee) is responsible for the oversight of these processes.

Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation to accomplish its objectives by bringing a systematic, disciplined approach to evaluating and improving the effectiveness of risk management, control and governance processes. The internal auditor is appointed by the Board, not by the CEO or Management Board, is not part of the management team and, unlike other employees, does not hold an operational role.

External (statutory or financial) auditing is the obligatory annual examination of a company's financial statements and records by an independent external auditor. The external auditor is approved by the shareholders on the recommendation of the Board.

Differences between the internal and external audit functions

ASPECT	INTERNAL AUDIT	EXTERNAL AUDIT
Who performs it?	Employees of the company or outsourced internal auditors	Independent third-party firm
Purpose	Improve internal operations, risk management, and controls; help the company achieve its goals	Provide an independent opinion on the fairness and accuracy of financial statements
Audience	Management and the Board and audit committee	Shareholders and other stakeholders (investors, creditors, regulators, public)
Scope	Broad; covers various aspects of the business (operations, compliance, IT, HR, cyber and other areas)	Primarily focused on financial statements and internal controls over financial reporting

ASPECT	INTERNAL AUDIT	EXTERNAL AUDIT
Reporting	Internal reports for the audit committee and the Board, with recommendations for improvement	Formal audit report, expressing an opinion on financial statements and presented to the audit committee, Board and shareholders
Independence	Organisational independence; not subordinate to the company's CEO or Management Board	Strict independence from the company being audited (no material ties, no provision of other services)
Mandatory?	Generally, not, but highly recommended for good governance	Usually legally mandatory
Frequency	Ongoing throughout the year	Typically, annual

Internal audit

Internal audit is a function within a company that is tasked with providing unbiased, independent reviews of systems and processes. That is why the internal auditor is the only non-operational function in the company. The role of internal audit is to provide the Board and top management with an objective source of information regarding the company's risks, control environment, operational effectiveness and compliance with applicable laws and regulations.

The reviews performed by Internal Audit are called internal audits. The aim of internal audits is to identify weaknesses within the organisation's processes and control environment internally so that they can be fixed as quickly as possible to prevent harm to the company or its stakeholders.[19]

Internal audit reports to the Board (and its audit committee), providing recommendations for the necessary improvements in systems and processes as well as reports on the implementation of those recommendations. It is important to emphasise that, where the Board has an audit committee, the Board should still maintain a regular relationship with the internal auditor and not delegate this important duty entirely to its audit committee, which supports the Board by examining internal audit activities in greater depth and providing opinions and suggestions for Board decisions.

It is important to emphasise that internal audit not only performs internal audits, but also advises the responsible company employees to help them achieve the set goals. Internal audit is the eyes and ears of the Board.

19 See also Linford & Co, Internal control environment, https://linfordco.com/blog/internal-control-environment/.

Internal audit should comply with the Global Internal Audit Standards of the IIA.[20]

The audit committee proposes, and the Board approves:

- the internal audit regulations;
- the strategic internal audit plan;
- the risk-based internal audit plan (three-year and annual);
- the internal audit budget (annually);
- the appointment, dismissal, evaluation and remuneration of the head of internal audit.

The head of internal audit must have functional accountability to the audit committee and the Board, and only administrative accountability to the CEO. It is the Board, not the CEO, that appoints the internal auditor, sets their remuneration and assesses their performance.

External audit

The responsibilities of the Board and its audit committee in relation to the external audit include:

1. ***Recommending the external auditor.*** The audit committee assesses potential audit firms (and the particular auditor) for independence, objectivity and expertise, and then recommends a firm (and the particular auditor) to the Board for appointment or reappointment by the shareholders.
2. ***Negotiating fees.*** The audit committee negotiates the auditor's fees to ensure that they are reasonable and will not compromise audit quality.
3. ***Reviewing the audit plan.*** The audit committee reviews and approves the external auditor's audit plan, including the scope of the work, the key risks identified and the planned resources.
4. The entire Board (including the audit committee) should ***meet the auditor twice*** during the annual audit cycle: before the audit, to share its insights into the situation in the company that could be relevant to the auditor and to learn about the audit plan, and after the audit, to discuss the findings and the auditor's report. ***In addition***, the audit committee should meet the auditor during the audit to discuss emerging findings.
5. The audit committee should ***assess the quality of the external auditor's work***.

20 The IIA (2024), Global Internal Audit Standards, https://www.theiia.org/en/standards/2024-standards/global-internal-audit-standards/.

6. Ensure that the external auditor is invited to the annual general meeting of shareholders.
7. The Board, with the help of its audit committee, should ***follow up on the external auditor's recommendations***.
8. The Board should ***ensure the disclosure of the audit report*** (in the annual report and on the website).
9. Ensure that the auditor is rotated in line with the applicable rules: for public-interest entities, EU law requires rotation of the audit firm after no more than ten years and of the key audit partner after no more than seven years, unless national legislation sets other limits.
10. Pay close attention to the smoothness of the collaboration between the executives and the auditor.

KEY TAKEAWAYS

A. Management is responsible for sound risk management and internal control systems; the Board, with the support of the audit committee, is responsible for their oversight. Internal audit and the external auditor are the Board's principal sources of independent assurance.

B. Internal audit is an independent, objective assurance and consulting function that evaluates and improves risk management, control and governance. It is appointed by the Board, not the CEO, reports functionally to the Board and its audit committee, and is the only non-operational function in the company.

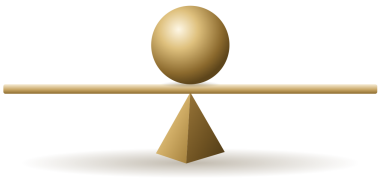
C. The audit committee proposes, and the Board approves, the internal audit regulations, the strategic and risk-based audit plans, the budget and the appointment, dismissal, evaluation and remuneration of the head of internal audit. Even with an audit committee, the full Board should maintain a direct relationship with the internal auditor.

D. External audit is the statutory annual examination of the financial statements by an independent auditor, approved by the shareholders on the Board's recommendation. The audit committee assesses the auditor's independence and quality, negotiates fees and reviews the audit plan.

E. The Board should meet the external auditor at least twice a year, follow up on the auditor's recommendations, ensure the audit report is disclosed and that rotation rules are observed, and watch the quality of the working relationship between executives and the auditor.

QUESTIONS FOR THE BOARD

1. *Does internal audit report functionally to the Board and its audit committee, and is it the Board, not the CEO, that appoints, evaluates and remunerates the head of internal audit?*
2. *Are the internal audit regulations, the strategic and annual risk-based audit plans and the budget approved by the Board, and do they cover the company's most significant risks?*
3. *How does the full Board, and not only the audit committee, engage with internal audit, and how are its recommendations followed up?*
4. *Has the audit committee assessed the external auditor's independence, expertise and quality of work, and are the fees adequate to secure a quality audit?*
5. *Did the Board meet the external auditor before and after the annual audit, and what did the auditor raise that management did not?*
6. *Are the auditor rotation requirements observed, is the auditor invited to the general meeting, and is the audit report disclosed in the annual report and on the website?*
7. *Does the relationship between executives and the auditor allow open and timely disclosure of issues, and would the Board know if it did not?*



CHAPTER

5.3

ETHICS AND INTEGRITY

How the Board sets and guards the company's ethical standard – from compliance and whistleblowing to conflicts of interest and related party transactions.

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5.3.1

ETHICS

Ethics is about doing what is right, not only what is required. The law and the corporate governance code set the minimum standards; ethics is the standard the company sets for itself, and the one by which its Board, management and people are judged when the rules are silent or inconvenient. Every company has an ethical standard in practice, whether or not it is written down. The question for the Board is whether that standard is chosen deliberately and upheld consistently, or left to emerge from habit and pressure.

This sub-chapter deals with the ethical standard itself and the Board's responsibility for it. Corporate culture and tone at the top are covered in sub-chapter 5.1.2; compliance, whistleblowing, conflicts of interest and related party transactions in sub-chapters 5.3.2 to 5.3.5; and the duty of loyalty of each Board member in sub-chapter 4.1.

Most corporate scandals begin not with an illegal act but with a series of lawful decisions that no one was willing to call wrong. Ethical failures destroy trust faster than financial ones. In the Baltic states, where markets are small and business and political networks overlap, the cost of an ethical lapse is high, and for state-owned and municipally owned enterprises public trust in the company is also public trust in its owner.

The role of the Board

The Board is the guardian of the company's ethical standard. It cannot delegate this role to a compliance function or a lawyer, because ethics is ultimately a matter of judgement, and the Board's judgement sets the ceiling for everyone else's. The Board's contribution has four parts. It defines the standard, by approving the code of ethics and the company's position on the dilemmas that matter in its business. It embodies the standard, by applying the same rules to itself and by the way it takes decisions. It tests the standard, by asking about the ethical dimension of what it approves and by refusing lawful but improper proposals. And it protects the standard, by ensuring that systems are in place to detect and correct breaches, and that consequences apply regardless of seniority.

Management runs the ethics programme: it drafts the code, designs training, handles day-to-day questions and investigates most incidents. The Board does not do this work, but it approves the framework, receives the evidence and holds management to account for the results. Where a Board committee exists, the audit committee or a dedicated ethics and compliance committee will usually prepare the

materials and proposals for the Board; the responsibility, however, remains with the full Board.

What the Board should do

1. **Own the ethical standard.** Approve a code of ethics (or code of conduct) that expresses the company's values in concrete terms, states what is expected of everyone from the Board down, and explains how to raise concerns. Keep it short and specific to the company; review it at least every three years and whenever the business changes materially.
2. **Apply the standard to the Board first.** Adopt Board-level rules on gifts and hospitality, outside interests, use of company information and dealings with shareholders, and record in the minutes that they are observed. A Board that exempts itself from the code cannot demand that management follows it.
3. **Make ethics a criterion in decisions, not an afterthought.** Require that major proposals to the Board (transactions, market entries, restructurings, incentive schemes and similar) address the ethical and reputational dimension explicitly: who is affected, what could go wrong, and how the decision would look if made public. Where a decision is lawful but questionable, the Board should be prepared to say no.
4. **Assign clear ownership.** Designate who is responsible for the ethics programme (an ethics or compliance officer, the company secretary or a committee) with direct access to the Board or its audit committee, adequate resources and the authority to investigate. In smaller companies the role can be combined with another function, provided the reporting line to the Board is preserved.
5. **Insist on training that is practical.** Ensure that all employees, and the Board itself, receive training built around real dilemmas the company faces, in the languages people actually speak, rather than a generic annual e-learning module. Ask to see the dilemmas used, not only the completion rates.
6. **Review ethical performance at least annually.** Receive a report covering incidents and how they were handled, questions raised with the ethics function, results of employee surveys on trust and pressure, and the disciplinary consequences applied at all levels. Treat this review with the same seriousness as the review of financial results.
7. **Verify consistency across the company, its group and the value chain.** Ensure that subsidiaries, agents, distributors and major suppliers are bound by equivalent standards, particularly where the company operates in markets or sectors with a higher risk of corruption, sanctions breaches or human rights violations.

Warning signs

- The code of ethics has not been revised for years and nobody on the Board can recall its main provisions.
- Ethical questions are referred to the legal department, and the answer is always “it is legal”.
- Board papers on major transactions or incentive schemes contain no reference to reputational or ethical risk.
- Reported incidents are few and always minor, while the company operates in a high-risk sector or market.
- Senior managers accept invitations, gifts or side engagements that would not be tolerated at lower levels.
- Employees describe the values as “what we say to customers” rather than “how we work”.
- Pressure from a shareholder, including a public owner, to take a decision the Board considers improper is accepted without a recorded discussion.

Common pitfalls and drawbacks

The first pitfall is confusing ethics with compliance: assuming that because the lawyers have cleared a decision, the ethical question has been answered. It has not; the law is the floor, and many of the decisions that later prove most damaging were perfectly lawful. The second is the aspirational code: a document full of fine words that gives no guidance on the three or four dilemmas that actually arise in the company’s business, such as gifts from suppliers, pressure from a large customer or shareholder, or cutting corners to meet a deadline. The third is the exception for the important: tolerating behaviour from a founder, a star salesperson or a politically connected manager that would end the career of a junior employee. Nothing tells the organisation more clearly what the real standard is. The fourth is treating ethics as a reporting line rather than a Board responsibility, so that the Board hears about it once a year in a slide on training completion. Boards should also be aware of the opposite risk: an ethics programme so heavy with policies, declarations and campaigns that people stop reading and start ticking boxes. A short code, honest examples and visible consequences work better than volume.

Guidance for other governance professionals

The company secretary should ensure that the code of ethics is formally approved and periodically reviewed by the Board, that ethics appears on the Board’s annual calendar, that Board members’ own declarations are collected and minuted, and that new directors are inducted into the company’s ethical standards and the

dilemmas specific to its business. The ethics or compliance officer should keep the code short and usable, build training around real cases, maintain a record of the questions and incidents raised, and report to the Board on patterns and root causes rather than on activity. Internal audit should test whether the standard is applied in practice, for example by reviewing gifts and hospitality registers, procurement decisions and the handling of past incidents, and should state in its findings where a control was bypassed for reasons of culture rather than capability. Human resources should ensure that ethical conduct is assessed in performance reviews and promotion decisions, and that disciplinary outcomes are consistent across levels. General counsel should advise on what the law requires, but should also be willing to tell the Board when a lawful course of action is nonetheless unwise.

KEY TAKEAWAYS

A. Ethics is about doing what is right beyond what the law requires. Compliance sets the floor; ethics sets the standard by which the company, its Board and its people are judged.

B. The Board is the guardian of the ethical standard. It approves and reviews the code of ethics, applies the code to itself first, and treats ethical and reputational considerations as a criterion in every major decision.

C. An ethical standard needs an infrastructure: clear ownership with a reporting line to the Board, practical training built on the company's real dilemmas, a safe channel for raising concerns (sub-chapter 5.3.3), and consistent consequences at all levels.

D. Ethics must be reviewed at least annually on the basis of evidence – incidents, questions raised, survey results and disciplinary outcomes – with the same rigour as financial performance

E. In the Baltic context, small markets, close personal networks and, in SOEs and MOEs, political pressure create specific ethical risks. The Board should name them openly and set rules for them, rather than assume goodwill.

F. Ethics extends beyond the company's own staff to subsidiaries, agents, distributors and suppliers, particularly in higher-risk markets and sectors.

QUESTIONS FOR THE BOARD

1. *Do we have a code of ethics that is specific to our company, approved and reviewed by the Board, and would it tell a new employee what to do in the three situations most likely to arise in our business?*
2. *Does the Board apply to itself the rules on gifts, hospitality, outside interests and confidential information that it expects management to follow, and have we, as directors, declared our own?*
3. *Is ethical and reputational risk assessed explicitly in the papers for major decisions, and which decision in the last year did we take, or refuse, mainly on ethical grounds?*
4. *Who owns the ethics programme, do they have the resources and authority to investigate, and do they report directly to the Board or its audit committee?*
5. *Who in this company would tell the Board that management has crossed an ethical line, and would they feel safe doing so?*
6. *Do our remuneration and promotion decisions reward the way results are achieved, or only the results, and are consequences for misconduct applied consistently regardless of seniority or performance?*
7. *What evidence did the Board review in the last year on ethical performance – incidents, questions raised, survey results, disciplinary outcomes – and what did it decide as a result?*
8. *What do our subsidiaries, agents, distributors and key suppliers know about our ethical standards, and how would we find out if they breached them?*
9. *For SOEs and MOEs: how does the Board handle requests from the owner that it considers improper, and is that handling recorded?*

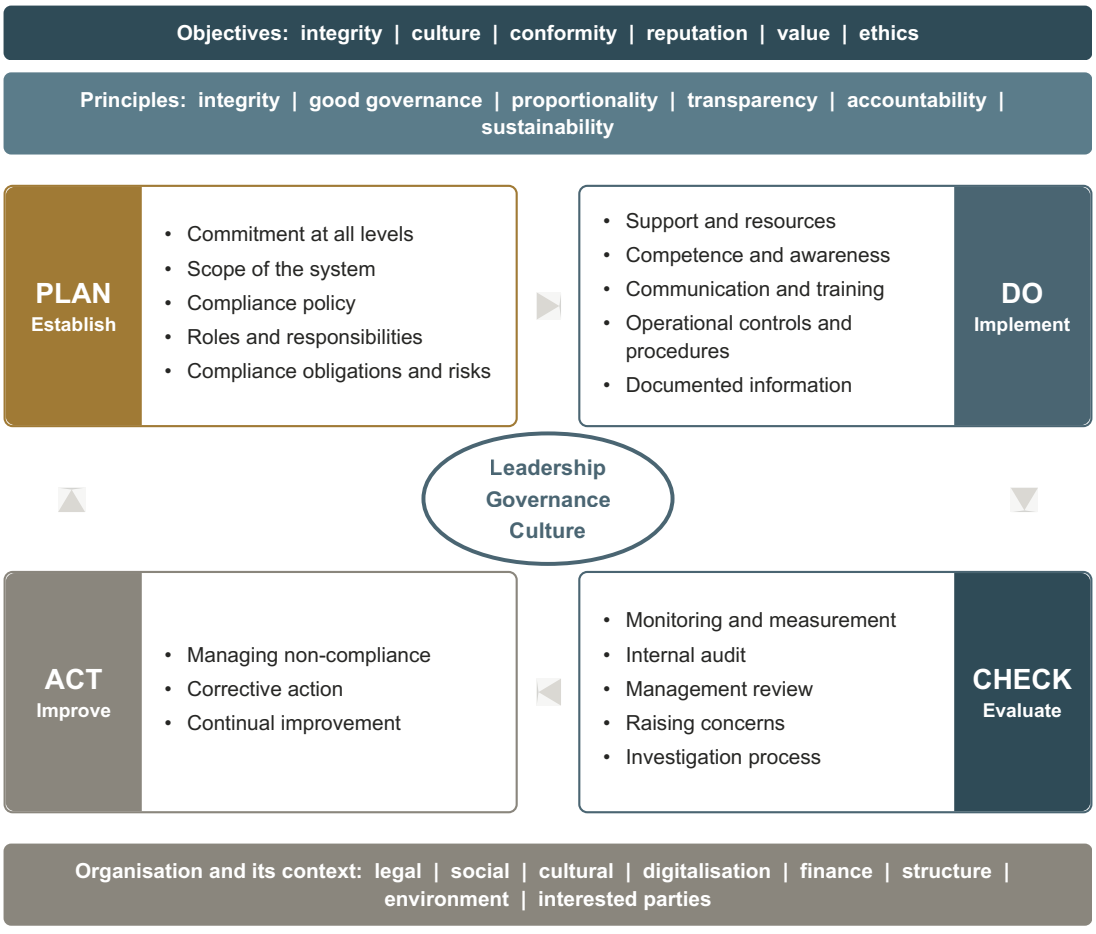
5.3.2
COMPLIANCE

With ever-evolving regulatory requirements, compliance risk is one of the key risks that every company, irrespective of its type, size or other characteristics, faces daily. Compliance risk is the risk of legal or regulatory sanctions, material financial loss or loss of reputation that a company may suffer as a result of its failure to comply with laws, regulations, rules, self-regulatory standards and codes of conduct.

To manage compliance risk, every company should maintain an effective compliance management system. For the system to be effective, it should not only implement policies and procedures to prevent and detect violations of the law, but also promote an organisational culture that encourages ethical conduct and a commitment to compliance with applicable laws, good governance and ethical standards.

The diagram below shows the main elements of a compliance management system as set out in the ISO 37301:2021 standard.

Figure 5.6 **Main elements of a compliance management system**



Source: BICG, based on the structure of ISO 37301:2021, Compliance management systems – Requirements with guidance for use.

A **compliance management system follows the plan - do - check - act cycle**. The company:

1. **plans the system** by securing commitment at all levels, defining its scope, adopting a compliance policy, allocating roles and responsibilities and identifying its obligations and compliance risks;
2. **puts the system into operation** through support, competence, communication, training, controls, procedures and documentation;
3. **checks the system** through monitoring and measurement, internal audit, management review, channels for raising concerns and an investigation process; and
4. **acts on the results** by managing non-compliance and improving continually. Leadership, governance and culture sit at the centre of the cycle, and the whole system is shaped by the company's objectives, its principles and its context.

Compliance is the outcome of a company meeting its obligations. Policies and procedures to achieve compliance should be integrated into all aspects of how the company operates. Compliance should not be treated as a stand-alone activity: it should be aligned with the company's overall strategic objectives and, while maintaining its independence, integrated with the company's financial, risk, quality, environmental and health and safety management systems and its operational procedures.

A company's approach to compliance should be shaped by its leadership, applying the company's core values and generally accepted governance, ethical and community standards.

In essence, compliance is a threefold duty covering:

1. the personal duty of Board members and employees to behave in accordance with the law and the company's rules;
2. the organisational duty of the governing bodies to set up and maintain a system that ensures that the company and its employees act in accordance with the law and the company's principles, and that breaches are discovered in a timely and efficient manner;
3. the duty of the members of the corporate bodies to pre-empt breaches and to avoid the resulting damage to the company's value.

A practical first step is to identify and map the compliance areas most relevant to the company and to establish, and keep up to date, a register of the external legal requirements and internal rules with which the company must comply.

The role of the Board

The Board approves the compliance policy and the appointment of a compliance officer or function with the independence, resources and authority to do the job, and with a direct reporting line to the Board or its audit committee. It sets risk-based priorities, receives regular reports on compliance risks, breaches, contacts with regulators and remediation, and ensures that the compliance function is integrated with risk management and internal audit under the Three Lines Model and operates effectively. In smaller companies the role may be combined with another function, provided that its independence and access to the Board are preserved.[AJ1.1]

Board roles and responsibilities

The Board is ultimately accountable for the company's compliance with law and ethical standards. This cannot be fully delegated - management implements, but the Board oversees and is responsible.

The Board's specific responsibilities include:

(i) Set the tone - demonstrate commitment to ethical behavior and compliance, including zero tolerance for corruption and misconduct.

(ii) Approve key policies - Code of Ethics, Anti-Corruption Policy, and Whistleblower Policy should be board-approved documents.

(iii) Engage in compliance risk oversight - understand the company's material compliance risks, satisfy themselves that appropriate mitigation measures are in place, and challenge management where controls appear inadequate.

(iv) Oversee compliance performance - receive and critically review periodic compliance reports and risk assessments; ask probing questions; and escalate concerns where red flags are not adequately addressed.

(v) Foster a compliance culture - actively promote company's culture in which ethical conduct is expected, reported concerns are taken seriously, and non-retaliation is guaranteed.

(vi) Ensure adequate resources - satisfy themselves that a competent, sufficiently independent compliance function (or Compliance Officer) exists with an adequate budget and clear reporting lines to the board.

(vii) Personal conduct - each board member must comply with conflict of interest obligations, insider trading rules (if applicable), confidentiality duties, and all other duties to which they are subject in their capacity as board members, including expected conduct under the Code of Ethics.

(viii) Incident oversight - serious compliance incidents and material whistleblower cases must be reported to the board, which should oversee investigation and remediation.

(ix) Board-level liability - directors may incur personal criminal or administrative liability for compliance failures. Ignorance of compliance obligations is not a defence — board members are expected to be and remain informed.

KEY TAKEAWAYS

A. Compliance risk is the risk of sanctions, financial loss or reputational damage from failing to comply with laws, regulations, self-regulatory standards and codes of conduct. Every company faces it daily, whatever its size or sector.

B. An effective compliance management system combines policies and procedures to prevent and detect breaches with a culture that encourages ethical conduct. ISO 37301:2021 provides a recognised reference model.

C. Compliance is a threefold duty: the personal duty of every Board member and employee to comply, the organisational duty of the governing bodies to set up a system that ensures compliance and detects breaches, and the duty to pre-empt breaches and avoid damage to the company.

D. Compliance is integrated into the way the company operates, aligned with its strategy and linked to its risk, quality, environmental and health and safety systems, while keeping the independence of the compliance function.

E. The Board approves the compliance policy, ensures that the compliance function has independence, resources and a direct line to the Board or its committee, and receives regular reporting on compliance risks, breaches and remediation.

QUESTIONS FOR THE BOARD

1. *Which laws, regulations and internal rules matter most for our business, and do we maintain an up-to-date register of them with named owners?*
2. *Has the Board approved regularly reviews a compliance policy and appointed a compliance officer with adequate resources, independence and direct access to the Board or its audit committee?*
3. *Does the compliance system prevent and detect breaches in practice, and what were the most significant compliance incidents, regulatory contacts and remediation actions in the last year?*
4. *Is compliance risk part of the risk register and risk appetite, and how does the Board satisfy itself that the compliance function is effective and not only documented?*
5. *Do Board members and management set the example in complying with the company's rules, and how does the company keep track of regulatory change?*

5.3.3

WHISTLEBLOWING

A whistleblowing mechanism is the structured, formal system that a company puts in place to allow employees, customers, suppliers, contractors and other stakeholders to report misconduct, illegal activities or unethical behaviour safely.

Whistleblowing addresses matters that affect the public interest or the integrity of the company. To distinguish whistleblowing from personal employment grievances, a whistleblowing framework applies to actions that threaten the company's integrity or the public interest, such as:

- Fraud, corruption, bribery or money laundering.
- Financial malpractice or deliberate breach of accounting controls.
- Breaches of environmental, health and safety regulations.
- Cover-ups or destruction of evidence related to any of the above.

The core goals of a whistleblowing mechanism are:

- Early detection. To act as an early-warning system that uncovers fraud, bribery and compliance breaches before they grow into corporate crises.
- Psychological safety. To create a "speak-up" culture where employees feel safe to voice concerns without fear of workplace bullying, demotion, or dismissal.
- Stakeholder trust. To build mutual trust by giving external stakeholders a transparent mechanism for identifying systemic risks, preventing ethical breaches and safeguarding the interests of investors, partners and the community.
- Accountability. To bypass traditional hierarchies so that misconduct at the executive or management level cannot be concealed.

The strategic benefits for the company are:

- Financial protection. Research consistently shows that occupational fraud is most frequently detected through tips. Early detection greatly reduces financial losses and helps to avoid regulatory fines.
- Reputational safeguarding. Handling issues internally and correcting them proactively reduces the risk of damaging leaks to the media or regulators.
- Improved culture. An active, trusted whistleblowing system signals to employees that management values integrity, boosting morale, trust and talent retention.

– Competitive advantage. Institutional investors increasingly treat robust environmental, social and governance (ESG) frameworks, including whistleblowing mechanisms, as a criterion in allocating capital.

The role of the Board and Management

The roles and responsibilities of the Board in whistleblowing:

1. Setting the tone at the top. The Board should publicly champion the whistleblowing system, making it clear that raising concerns is an act of loyalty to the company.
2. Whistleblowing policy. The Board approves and regularly reviews a whistleblowing policy establishing a formal infrastructure: secure reporting channels (hotlines, web platforms), independent investigators (where appropriate, external service providers) and strict non-retaliation rules.
3. Ensuring independent reporting lines. The Board (typically through its audit committee) should ensure that the whistleblowing process is functionally independent of executive management, to prevent conflicts of interest.
4. Direct escalation route. The policy should provide fast-track reporting for high-risk cases: a report concerning senior management goes directly to the Chair of the Board or the audit committee, so that the subjects of an investigation can never oversee it.
5. System monitoring and key indicators. The Board (with the help of its audit committee) regularly reviews anonymised metrics on the reporting system (number of reports, categories of misconduct, investigation closure rates). A complete absence of reports should be challenged by the Board as a possible sign of a culture of fear.
6. Protecting the whistleblower. The Board safeguards the speak-up culture by holding management responsible for the well-being of those who report, and verifies that protection measures are effective and that any retaliation is met with immediate corrective action.

The roles and responsibilities of management in whistleblowing:

1. Establishing accessible channels. Management provides secure, accessible and easy-to-use channels (such as external 24/7 hotlines or encrypted web platforms) that allow anonymous or strictly confidential reporting.
2. Drafting and enforcing procedures. Management creates clear, transparent written procedures detailing how reports are received, how investigations are conducted and how feedback is given to the reporter.

3. Appointing competent case handlers. Management designates and empowers impartial, trained individuals or functions (such as compliance) to handle incoming reports objectively. It is recommended to appoint an independent third-party provider to host the intake hotline or digital platform; this significantly increases employee trust and ensures that reporting data cannot be traced by the internal IT department and that reports are investigated independently.
4. Awareness and training. Management is responsible for continuously training staff on how to use the system and for educating managers on how to react appropriately when an employee raises a concern.
5. Taking corrective action. When an investigation confirms wrongdoing, management takes appropriate disciplinary action and updates internal controls to prevent recurrence.
6. Reporting to the Board and its audit committee. Management provides regular anonymised reports that allow the Board to fulfil its oversight duty.

The core conditions for whistleblowing to succeed are:

- Confidentiality and anonymity. The identity of the whistleblower must remain strictly confidential and be shared only on a need-to-know basis with those conducting the investigation. Anonymous reporting must be fully supported.
- Impartiality. Every report must be assessed objectively by a trained professional who has no personal or professional conflict of interest with the subject of the report.
- Timely feedback. The system must acknowledge receipt of reports promptly and provide the reporter with status updates within a reasonable, predefined timeframe.
- Actionable outcomes. Whistleblowing must yield tangible results; management must follow through with concrete disciplinary actions when wrongdoing is proven.
- Transparency. The whistleblowing policy and the reporting channel or form should be freely available on the company's external website (reachable from its home page). This demonstrates transparency to all stakeholders and ensures that external parties and former employees can easily access the channels.
- Tone in the middle. While the Board sets the tone at the top, management must ensure that middle managers and supervisors support the policy, translating ethical values into daily operational behaviour so that employees feel safe raising issues at departmental level.

Compliance with EU rules

When establishing or improving a whistleblowing framework, companies must ensure that it complies with the EU Whistleblowing Directive, as transposed in Estonia, Latvia and Lithuania, and with the GDPR, so that reports are handled lawfully and personal data are protected. The Directive requires companies with 50 or more employees to establish internal reporting channels and procedures.[21]

KEY TAKEAWAYS

A. A whistleblowing mechanism is a formal system that allows employees and external stakeholders to report misconduct, illegal activity or unethical behaviour safely. Its purpose is early detection, a speak-up culture, stakeholder trust and accountability that bypasses hierarchy.

B. The Board sets the tone, approves the whistleblowing policy, ensures the process is independent of executive management, provides a direct escalation route to the Chair or the audit committee for cases involving senior management, reviews anonymised metrics and protects those who report.

C. Management provides accessible and secure channels, clear procedures, impartial and trained case handlers (preferably with an independent external provider for intake), training, corrective action and regular reporting to the Board.

D. Whistleblowing succeeds only with confidentiality and anonymity, impartiality, timely feedback, actionable outcomes, transparency of the policy and channels, and support from middle management.

E. In the EU, the framework must comply with the Whistleblowing Directive, as transposed nationally, and with the GDPR; companies with 50 or more employees must have internal reporting channels.

21 Directive (EU) 2019/1937 on the protection of persons who report breaches of Union law (the Whistleblowing Directive).

QUESTIONS FOR THE BOARD

1. *Do we have a Board-approved whistleblowing policy and secure channels that are known to employees and accessible to external stakeholders, including through our website?*
2. *Is the process independent of executive management, and would a report concerning the CEO or a Board member reach the Chair or the audit committee directly?*
3. *What did the last year's anonymised metrics show (number of reports, categories, closure times), and if there were no reports, why?*
4. *How do we know that whistleblowers are protected from retaliation, and what happened in the last case where someone raised a concern?*
5. *Do our channels and procedures comply with the national law transposing the EU Whistleblowing Directive and with the GDPR, and when were they last reviewed?*
6. *Does management, including middle management, treat raising concerns as an act of loyalty, and how does the Board know?*

5.3.4
CONFLICT OF INTEREST

A conflict of interest (***COI***) is a situation in which two or more parties have competing interests which may, actually or potentially, improperly influence a decision-making process and make it difficult for those involved to fulfil their duties fairly. In general terms, a COI exists where the interests of two parties collide, so that satisfying one is at the expense of the other.

In the context of Board work, a COI is a situation in which a Board member's personal, financial or other interests interfere, or could interfere, with their duty to act in the best interests of the company, thus compromising, or appearing to compromise, their ability to make impartial decisions on the company's behalf.

A conflict of interest typically arises when personal interests are placed above those of the company, and it usually materialises in the decision-making process. It may involve one party being able to take a decision affecting another, or holding or having access to information about another, where the decision or the information can benefit or harm the deciding or receiving party or a person related to it, and generally carries a risk of violating the rights of the other party.

Conflicts of interest are not in themselves illegal or prohibited. To ensure that they do not lead to corrupt practices, which may be subject to investigation and prosecution with serious legal, financial and reputational consequences, they must be disclosed, prevented, mitigated or managed.

Types of conflict of interest

A COI can be (i) actual, (ii) potential or (iii) perceived, and can arise in a wide variety of ways:

Actual COI: the person is influenced by a conflict of interest

An actual COI is a situation in which the circumstances clearly constitute a conflict: a Board member or another person related to the company faces a real and existing conflict of interest. For instance, the following situations constitute an actual COI:

- Serving on the Board of the company while also serving on the Board of a competitor or of a service provider of the company;
- The company entering into a transaction with a Board member or their related party;
- Hiring or supervising a relative, spouse, cohabitee or close friend;

- Using company assets for private benefit;
- Close personal relationships influencing decisions taken as part of the Board role;
- Using confidential information obtained in the role for one's own benefit.

Potential COI: the person could be influenced by a conflict of interest

A potential COI is a situation that does not yet constitute a conflict but where there is a reasonable possibility of an actual or apparent conflict arising. For instance:

- A person serves on the Boards of two companies that have no business relationship; a COI may arise if the two companies plan to do business together;
- Serving on several Boards, within or outside the group, which takes up a significant amount of time and raises the question whether the person can fulfil all of their duties and, if not, which will be prioritised;
- A Board member is a former official of a public authority; a COI could arise if the company becomes subject to an investigation by that authority;
- A Board member of company A also serves on the Board of company B, a client of company A; a COI could arise if company B were to file a complaint against company A.

Perceived COI: the person could appear to be influenced by a conflict of interest

A perceived conflict is a situation in which a person appears to have a COI even though this is not the case. For instance, the company hires a new employee who has the same surname as the CEO although they are not related.

Managing conflicts of interest

In performing their duties, Board members must act fairly and reasonably and be loyal to the company, without preference for the interests of any shareholder or group of shareholders, even if the Board member was nominated and appointed by that shareholder or group.

Proper management of conflicts of interest involves at least the following:

1. **Effective COI policy and processes.** The Board is responsible for ensuring that the company has effective procedures to identify, evaluate, prevent and mitigate conflicts of interest. The Board should approve the COI policy, regularly revise it and oversee its implementation. The policy should be reviewed at least every three years and whenever it becomes apparent that the processes it establishes are not effective.

2. **Training.** The company should organise initial training (on induction) and regular refresher training on conflicts of interest for the Board and employees, so that everyone is reminded of their obligation to identify and manage them and new recruits are informed in a timely manner.
3. **Declaration of interests.** Board members, senior management and key personnel must (i) declare their related parties (close family members and entities in which they or their close family members have a material holding, votes or influence), other positions and employments held currently or during the last three to five years, and any other material interests and affiliations that could influence their independence of mind in performing their duties; and (ii) update this information regularly (quarterly or annually) and whenever changes occur.
4. **Declaration of a COI.** Where a COI may arise in a specific situation (for example, the company intends to sign a contract with an entity controlled by a Board member), the Board member must declare the existence and nature of the potential conflict to the Chair and the Board without delay upon becoming aware of it. Best practice is to declare it as soon as the member learns that the matter is on the Board's agenda and before the Board materials on the matter are distributed.
5. **Checking for a COI.** Management preparing an agenda item, and the corporate secretary checking the materials before the Board pack is distributed, should check against the declarations of interests whether a COI may exist and, if so, advise the Chair accordingly. At the beginning of each meeting the Chair asks whether any member may have a COI in respect of any agenda item.
6. **Decision on the existence of a COI.** Upon declaration or identification of a possible COI, the Board evaluates the nature and circumstances of the situation and the interests disclosed and decides whether a COI exists. If it does, the Board evaluates its materiality and decides on the measures to prevent, mitigate or manage it.
7. **Recusal.** A Board member who has a COI must recuse themselves from the consideration of, and voting on, the agenda item concerned. Recusal means that the information and Board materials on the matter are not shared with the member, that the member does not take part in its consideration (including leaving the meeting while it is discussed), so that the non-conflicted members can discuss it freely and without bias, and that the member does not vote on it.
8. **No influence on the decision.** The Board member must not seek to influence in any other way the decision on the matter in which they have a COI.
9. **Documentation.** The declaration, identification and evaluation of a COI, the decision on its existence and the measures taken to prevent, mitigate or

manage it should be documented. It is also recommended to draw up separate minutes recording the discussion and decision on a matter in which a Board member has a potential COI. Such minutes are reviewed, approved and signed by, and available to, the non-conflicted members; the conflicted member is informed of the decision and has access only to the resolution part of the separate minutes.

10. **COI register.** The company should keep an up-to-date register of conflicts of interest and the measures taken to manage them.
11. **Continuing COI.** *A* COI of a continuing rather than one-off nature, and the measures taken to manage it, should be regularly revisited, re-evaluated and, if necessary, adjusted to ensure that they remain sufficient and effective. A continuing COI may arise, for example, from a long-term service contract between the company and an entity controlled by a Board member's spouse. Where a continuing COI would require the member to recuse themselves from most of the matters discussed by the Board (for example, advising or serving on the Board of a competing business), this should be assessed before the appointment, and the person should not be appointed, since constant recusal would prevent them from performing their duties.

KEY TAKEAWAYS

A. A conflict of interest arises when a Board member's personal, financial or other interests interfere, or could interfere, with their duty to act in the best interests of the company. Conflicts may be actual, potential or perceived, and are not illegal in themselves, but must be disclosed and managed.

B. Board members act loyally to the company and without preference for any shareholder, including the one that nominated them.

C. Managing conflicts requires a Board-approved policy, training, declarations of interests by Board members and key personnel, prompt declaration of a conflict when it arises, checks by management and the corporate secretary before each meeting, and a Board decision on whether a conflict exists and how to manage it.

D. A conflicted member recuses themselves from the materials, discussion and vote and does not seek to influence the decision in any other way; the process and decision are documented, with separate minutes where appropriate, and recorded in a COI register.

E. Continuing conflicts are revisited regularly; a conflict that would require constant recusal should rule out the appointment in the first place.

QUESTIONS FOR THE BOARD

1. *Do we have a Board-approved conflict of interest policy, when was it last reviewed, and are Board members and key personnel trained on it?*
2. *Have all Board members and senior managers submitted declarations of interests, and are they updated regularly and when circumstances change?*
3. *How is each Board agenda checked for potential conflicts before the materials are distributed, and does the Chair ask about conflicts at the start of every meeting?*
4. *When a conflict was last declared, did the member recuse themselves fully, and was the decision documented and recorded in the COI register?*
5. *Do any Board members have continuing conflicts, and are the measures taken to manage them still sufficient?*
6. *Does any Board member act, or appear to act, in the interest of the shareholder that nominated them rather than of the company?*

5.3.5

RELATED PARTY TRANSACTIONS

Related party transactions (RPTs) are one of the situations in which a COI is inherent. RPTs are usually legitimate transactions between the company and a related party. A problem arises where such a transaction allows the related party to extract more value from the company than it would otherwise be entitled to (for example, a majority shareholder being paid above the market price for goods it sells to the company).

The Board should approve the related party transaction policy, regularly revise it and oversee its implementation.

Related party

Although the definitions in national regulations differ in detail, for the purposes of RPT governance the concept of a related party usually includes at least the following persons:

1. a direct or indirect controlling shareholder of the company, or any other person that, through shareholding or otherwise, has sole or joint control or significant influence over the company;
2. a member of the Board or of the key management personnel of the company or its affiliated entities;
3. close relatives of the persons listed in (1) and (2);
4. the holding, subsidiary and other affiliated entities of the company and of the persons listed in (1) to (3).

Related party transaction

A related party transaction is any arrangement involving a transfer of value (resources, services, rights or obligations) between the company and a related party, irrespective of whether a price is charged.

RPT governance

RPT governance aims to distinguish, and prevent, RPTs that are unfair to the company, to its shareholders generally or to minority shareholders from transactions that benefit the company and enhance its value. Although national regulations differ,

good corporate governance requires at least the following standards in respect of RPTs:

1. **Sufficient information.** Management provides the approving body with sufficient information on the terms and conditions of the proposed transaction.
2. **Audit committee opinion.** The opinion of the Board's audit committee (if the company has one) on the proposed RPT is obtained before the Board approves it. Committee members with a potential COI in respect of the RPT recuse themselves from its consideration and the vote, and follow the other principles of COI management.
3. **Board approval.** The RPT is approved by the Board in accordance with the RPT policy. Board members with a potential COI in respect of the RPT recuse themselves in the same way.
4. **Approval conditions.** When considering and approving an RPT, the audit committee and the Board must ensure that:
    i. the transaction is at *arm's length*; if it is not, the approving body must evaluate and justify that the RPT is *in the best interests* of the company and is *not unfair* to the shareholders unrelated to it. Before approving the RPT, the audit committee or the Board may obtain an independent qualified third-party opinion on the fairness of the transaction (a *"fairness opinion"*);
    ii. **the same internal procedures** have been followed for the evaluation, approval and monitoring of the RPT as for any other third-party transaction;
    iii. continuing RPTs (for example, the provision of services over a period of time, as opposed to one-off purchases) are regularly revisited, including:

    – regular reporting on and monitoring of the performance of the RPT;

    – regular re-evaluation and re-approval of the transaction, to ensure that it continues to be at arm's length, fair and in the best interests of the company; and

    – a change of its terms, or its termination, where it can no longer be justified as fair or as serving the interests of the company.

5. **Disclosure.** RPTs are disclosed in the company's financial statements and annual report.

Transactions with related parties entered into in the ordinary course of business and on market terms, and non-material transactions, are usually excluded from prior evaluation and approval. The permitted exclusions should be defined in the RPT policy and comply with national regulatory requirements, and summary information

on such transactions should be reported regularly to the Board (for example, in the regular compliance reports).

KEY TAKEAWAYS

A. Related party transactions are transfers of value between the company and a related party: a controlling shareholder, a member of the Board or key management, their close relatives, or affiliated entities. They are usually legitimate but carry an inherent conflict of interest.

B. The Board approves an RPT policy, revises it regularly and oversees its implementation. Its purpose is to prevent transactions that are unfair to the company, its shareholders generally or minority shareholders.

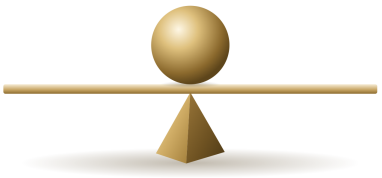
C. Before approval, management provides sufficient information, the audit committee gives its opinion, conflicted members recuse themselves, and the Board satisfies itself that the transaction is at arm's length or otherwise justified as being in the company's best interests, if necessary, with an independent fairness opinion.

D. RPTs follow the same procedures as any third-party transaction, continuing RPTs are re-evaluated and re-approved regularly, and RPTs are disclosed in the financial statements and annual report.

E. Ordinary-course, market-terms and non-material transactions may be excluded from prior approval if the policy so provides and the law allows, but summary information on them is still reported to the Board.

QUESTIONS FOR THE BOARD

1. *Do we have a Board-approved related party transaction policy that defines related parties, approval thresholds and permitted exclusions in line with national law?*
2. *Which related party transactions did the Board approve in the last year, and for each, how did it satisfy itself that the terms were at arm's length or otherwise in the company's best interests?*
3. *Did the audit committee give its opinion before approval, and did all conflicted members recuse themselves from the materials, discussion and vote?*
4. *Which continuing related party arrangements exist, when were they last re-evaluated, and are they still fair to the company?*
5. *Are related party transactions fully disclosed in the financial statements and annual report, and does the Board receive summary reporting on the transactions excluded from prior approval?*



CHAPTER

5.4

TECHNOLOGY AND INNOVATION

How the Board oversees digital transformation, the use of AI and the company's capacity to innovate.

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5.4.1

DIGITAL TRANSFORMATION AND AI

Companies have recognised the importance of digital transformation for staying competitive, improving efficiency and meeting customer expectations. Today every company is involved in digitalisation to some extent, and the role of the Board is to lead and oversee the digital transformation of the company and to ensure that:

- digital transformation is aligned with the company's long-term vision and strategic objectives;
- digital initiatives are integrated into the overall business strategy;
- resources are used efficiently;
- it strengthens the company's competitive advantages and creates long-term value.

The Board plays a key role in setting the strategic direction of digital transformation, overseeing the process and ensuring that the transformation is aligned with the overall goals and interests of the company.

It is important to emphasise that the Board itself must ensure that it possesses the competencies required for digital transformation. If needed, additional Board members should be recruited to bring the essential competencies, experience and know-how to the Board.

The Board's role in digital transformation and its oversight has several aspects:

1. ***Setting the strategic direction of digital transformation.*** The Board defines the company's overall strategy, including its approach to digital transformation. This requires a clear view of the potential impact of digitalisation on the company's industry, and guidance to the company in implementing a digitalisation strategy that improves operations and enhances competitiveness.
2. ***Risk governance.*** Digital transformation usually involves significant change, the introduction of new technologies and adaptation to an evolving business environment. The Board must ensure that the related risks are identified, assessed and properly managed, and that the company's digital initiatives are aligned with its risk appetite and compliance requirements.
3. ***Resource allocation and ensuring the required capacity.*** The Board approves the budgets and resources for digital transformation initiatives and needs to ensure that the necessary financial, human and technological resources are available to support successful implementation.

4. ***Talent and leadership development.*** The Board should pay attention to the development and recruitment of leaders with digital expertise. This includes hiring executives who understand digital technologies and can drive the transformation agenda. The organisational structure should also be reviewed and adjusted where necessary. The Board may also encourage a culture of continuous learning, to ensure that the Board itself and the existing leadership are well equipped for the digital age.
5. ***Monitoring progress. The*** Board must set clear goals and establish key performance indicators (KPIs) to measure the progress of digital initiatives and assess the success of the transformation. It should receive regular updates and reports on the status of digital transformation projects, allowing it to assess how effectively the digitalisation strategy is being implemented and to make informed decisions.

Digital transformation initiatives are complex and require new competencies, many changes and substantial resources. It is no surprise that many of them fail. Common reasons for failure include:

- Lack of a clear strategy and vision, and of their communication to employees and stakeholders.
- Resistance to change and to the adoption of new technologies and processes.
- Insufficient skills at Board and management level.
- Poor integration of new technologies with existing systems.
- Poor data quality and governance, leading to inaccurate insights and decisions, and the lack of a data-centric culture and of an understanding of the value of data.
- Inadequate cybersecurity measures and protocols, leading to vulnerabilities and a failure to address the security risks associated with new technologies and data storage.
- Budget overruns, poor financial planning and underestimation of the costs of digital transformation projects.
- Lack of a customer-centric approach: focusing on technology rather than on understanding and meeting customer needs and expectations.
- Poor project management practices, including inadequate planning and monitoring.
- Failure to set realistic timelines and milestones.
- Difficulties in managing relationships with technology vendors and service providers, and over-reliance on external partners without ensuring alignment with the company's goals.

- Failure to establish key performance indicators (KPIs) and metrics for evaluating the success of digital transformation.
- Inability to measure and demonstrate the return on investment (ROI).

The Board needs to ensure that the digital transformation adheres to legal and ethical standards. Compliance with regulations on data protection, security, artificial intelligence and other relevant areas must be a priority.

Artificial intelligence

Artificial intelligence has become a matter for the Board, not only for management. The Board's role is oversight and strategic alignment, while management is responsible for the day-to-day execution of AI projects. In practice this means five things: approving an AI policy that sets the company's principles for the responsible use of AI (purpose and scope, governance and accountability, risk management, ethical standards such as fairness, transparency and human oversight, data governance and regulatory compliance) and aligning AI initiatives with the business strategy; approving the budgets and resources for AI and ensuring that the company has the infrastructure and the talent to deliver; ensuring that AI-related risks, including bias, privacy, security and legal liability, are assessed and managed within the company's overall risk management framework and that the requirements of the EU Artificial Intelligence Act are met; setting clear KPIs to evaluate the return on AI investments and reviewing progress regularly; and overseeing the impact on employees, the organisational culture and other stakeholders, including the training of the Board itself.

A useful distinction for the Board is that between automation, which follows fixed rules and mainly requires monitoring of efficiency and reliability, and AI, which learns from data and therefore calls for a more demanding governance framework. BICG's Guidelines for Integrating Artificial Intelligence into the Board Agenda provide a fuller treatment, including a Board-level AI governance checklist, an opportunities and risks matrix and an implementation roadmap.[22]

In summary, the Board plays a pivotal role in guiding and overseeing the digital transformation, ensuring that it is aligned with the company’s strategic objectives, managing risks, allocating resources and fostering a culture that supports innovation and adaptability in the digital era.

22 Baltic Institute of Corporate Governance, Guidelines for Integrating Artificial Intelligence (AI) into the Board Agenda, BICG Policy Group Lithuania, [2026], available at www.bicg.eu.

KEY TAKEAWAYS

A. Every company is digitalising to some extent. The Board leads and oversees the digital transformation and ensures that it is aligned with the long-term vision and strategy, integrated into the business strategy, resourced efficiently and focused on competitive advantage and long-term value.

B. The Board must have, or acquire, the competencies to do this: through the recruitment of Board members with digital expertise and through continuous learning.

C. The Board's role has five aspects: setting the strategic direction, risk governance, resource allocation, talent and leadership development, and monitoring progress through clear goals, KPIs and regular reporting.

D. Many digital initiatives fail for predictable reasons: unclear strategy, resistance to change, insufficient skills, poor integration and data quality, weak cybersecurity, budget overruns, a technology-first rather than customer-first approach, poor project management and over-reliance on vendors.

E. Digital transformation must comply with legal and ethical standards, including data protection, security and the emerging rules on artificial intelligence.

F. Artificial intelligence is a Board matter: the Board approves an AI policy, ensures that AI risks are managed within the risk management framework and that the EU AI Act is complied with, sets KPIs for AI investments and oversees the impact on people and culture.

QUESTIONS FOR THE BOARD

1. *Is our digital strategy part of the company strategy, and can the Board explain how digitali transformation changes our industry and our competitive position?*
2. *Does the Board have sufficient digital competence to challenge management, and if not, how will we close the gap?*
3. *Which digital transformation projects are under way, what are their goals and KPIs, and how do they perform against budget and timeline?*
4. *Are the risks of digital transformation, including cybersecurity, data quality and dependence on vendors, in the risk register and within our risk appetite?*
5. *Do we have the leadership, skills and organisational structure to deliver the transformation, and is the culture supporting rather than resisting it?*
6. *Where does the company use or plan to use artificial intelligence, and how do we ensure that its risks are managed and legal requirements met?*

5.4.2

R&D AND INNOVATION

Research and development (R&D) and innovation are two crucial activities that contribute strongly to a company's competitive advantage, market differentiation, revenue growth, cost efficiency, customer experience, brand, risk mitigation and overall success.

The Board plays a vital role in guiding and overseeing the company's R&D and innovation activities. Its responsibilities include:

1. Setting the strategic direction. The Board aligns R&D and innovation efforts with the company's long-term objectives, including the goals and priorities for R&D and innovation.
2. Approving budgets. The Board approves the budgets for R&D and innovation activities in line with the company's goals.
3. Providing support and resources. The Board supports R&D efforts by ensuring access to the necessary resources, such as talent (internal and external) and infrastructure. The Board should approve strategic partnerships that contribute to the achievement of the company's innovation goals.
4. Oversight and risk management. The Board oversees R&D and innovation activities to ensure that they are conducted in a manner consistent with legal, business and ethical standards. This includes managing the risks associated with R&D and innovation investments and projects, and ensuring that appropriate controls are in place.
5. Monitoring performance. The Board monitors the performance of R&D and innovation initiatives, assessing progress towards strategic objectives and evaluating the return on investment. This may involve reviewing key performance indicators, milestones achieved and financial metrics related to R&D and innovation.
6. Fostering a culture of innovation. The Board should ensure that top management fosters a culture of innovation within the company, encouraging creativity, experimentation and knowledge sharing among employees.
7. Identifying emerging technologies and trends. The Board should stay informed about emerging technologies, market trends and competitive dynamics that may affect the company's R&D and innovation strategy, and may provide guidance on adapting to changing market conditions and seizing new opportunities.

8. Holding top management accountable. The Board should hold top management accountable for the company's R&D and innovation performance, ensuring that resources are managed effectively and strategic objectives achieved. Effective communication between the Board and the top management team is essential for this oversight.

Three questions come up repeatedly in Board discussions of R&D and innovation and deserve a closer look.

Balancing incremental and disruptive innovation. Most of a company's innovation effort goes into incremental improvements to existing products, processes and services: these are lower in risk, closer to customers and easier to measure. Disruptive innovation, which creates new business models or markets, is rarer, riskier and slower to pay back, but it is what protects the company from being overtaken. The Board's task is not to choose between the two but to make sure that the portfolio is deliberately balanced. A practical approach is to ask management to present R&D and innovation projects as a portfolio, sorted by time horizon (short, medium and long term) and by level of risk, and to agree what share of resources should go to each category given the company's strategy, its position in the industry and the pace of change around it. A company whose portfolio contains only incremental projects is usually under-investing in its future; one with only ambitious projects is usually over-estimating its ability to deliver them. The Board should revisit the balance at least once a year and whenever the strategy changes.

Protecting intellectual property. The results of R&D are worth little if they can be freely copied. The Board should satisfy itself that the company has an intellectual property strategy that fits its business: what should be patented, what is better kept as a trade secret, which trademarks and designs should be registered and in which markets, and how software, data and know-how are protected. Equally important are the contracts through which intellectual property flows: employment and contractor agreements should assign to the company the rights in what is developed for it, and agreements with partners, universities and suppliers should state clearly who owns the results of joint work. The Board should also ensure that the company respects the rights of others, since infringement claims can be as damaging as the loss of the company's own rights, and it should receive a periodic overview of the intellectual property portfolio, its value and any disputes.

Comparing R&D spending with peers. There is no correct level of R&D spending; the right amount depends on the sector, the strategy and the stage of the company. What the Board can and should do is compare. Useful benchmarks are R&D expenditure as a share of revenue, the split between research and development,

the proportion spent on incremental as opposed to new products, and the share of revenue that comes from products introduced in the last three to five years, each compared with listed competitors, sector averages and the company's own history. Public sources are often sufficient: the annual reports of listed peers, sector studies and the EU Industrial R&D Investment Scoreboard. The purpose of the comparison is not to match the peers but to explain the difference: a company that spends well below its sector should be able to say why that is consistent with its strategy, and one that spends well above should be able to show the results.

KEY TAKEAWAYS

A. R&D and innovation are crucial to competitive advantage, market differentiation, growth, efficiency, customer experience and brand, and also to risk mitigation.

B. The Board sets the strategic direction for R&D and innovation, approves the budgets, ensures the resources and strategic partnerships needed, and oversees that activities meet legal, business and ethical standards with appropriate controls.

C. The Board monitors performance through key performance indicators, milestones and return on investment, and holds top management accountable for results.

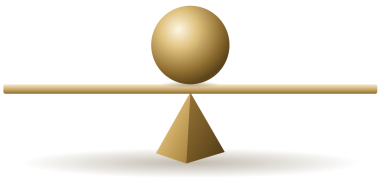
D. The Board should ensure that management fosters a culture of innovation, encouraging creativity, experimentation and knowledge sharing.

E. The Board should stay informed about emerging technologies, market trends and competitive dynamics, so that it can guide the company in adapting and seizing opportunities.

F. The Board judges the innovation portfolio as a whole, balancing incremental and disruptive projects by time horizon and risk; it ensures that the company's intellectual property is protected and the rights of others respected; and it compares R&D spending and results with peers to test whether the level of investment fits the strategy.

QUESTIONS FOR THE BOARD

1. *What are our innovation goals and priorities, and how are they linked to the company's long-term strategy?*
2. *How much do we invest in R&D and innovation compared with our competitors, and what has that investment delivered in the last three years?*
3. *Which KPIs and milestones does the Board use to monitor R&D and innovation, and when did it last review them?*
4. *Do we have the talent, partnerships and infrastructure needed for our innovation goals, and is our intellectual property protected?*
5. *Does the company culture encourage experimentation and tolerate well-managed failure, and how does the Board know?*
6. *Which emerging technologies or market trends could disrupt our business, and what is management doing about them?*
7. *Is our innovation portfolio deliberately balanced between incremental improvements and more ambitious projects, and when did the Board last review that balance?*



CHAPTER

5.5

LEADERSHIP AND REMUNERATION

How the Board selects, motivates, evaluates and plans the succession of the CEO, and how it oversees remuneration across the company.

IN THIS SECTION

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5.5.2	Remuneration of the CEO, management and employees	172

5.5.1

THE CEO: SELECTION, MOTIVATION, EVALUATION AND SUCCESSION

One of the main functions of the Board is to select and appoint the most suitable CEO, to make sure that the CEO is properly motivated, evaluated and remunerated, and to replace the CEO if the results are unsatisfactory, the CEO retires or other circumstances, such as illness or death, make a change necessary.

Selection and appointment process

The nomination and appointment process is key to strong company performance and effective accountability. In a well-run company, the selection of candidates for the CEO position is therefore best conducted through the Board's nomination committee, where one exists, or by the Board itself. The task of the committee is to carry out the selection process for the appointment and re-appointment of the CEO (and other senior managers) and to make recommendations to the Board.

The CEO must be selected on the basis of the company's stage of development, future plans and ambitions. The profile will differ considerably depending on whether the company is in a start-up, growth, mature, turnaround or distress phase. The requirements for the CEO should be based on the company's current and expected needs.

When preparing the search for a new CEO, the Board or its nomination committee must weigh the merits of an internal candidate against those of an external one. Selecting an **internal candidate** may bring continuity and stability, better alignment with the long-term goals, familiarity with the company's culture and internal processes and stronger internal networks. An **external candidate** may bring a fresh perspective, an objective assessment of the company's challenges, the ability to drive change, wider business networks, and specialised expertise and experience that the company needs at that particular time. In each case the Board has to consider the long-term goals of the company, its stage of development and the qualities the new CEO will need.

There are several important aspects to consider when onboarding a newly appointed CEO:

- Onboarding process – a structured introduction is one of the most critical factors in helping a new CEO to work at full speed as soon as possible.
- Regular feedback – make sure that the new CEO receives the right information early; do not wait until things have gone too far before raising an issue.

- Tolerance of mistakes – no one is immune to mistakes, least of all a person who has just joined the company.
- Respecting roles – avoid the temptation to micro-manage or to solve problems that are the CEO's responsibility.
- Dealing with negative information and rumours – there will naturally be some displeased subordinates, and some of them may even try to undermine the new CEO by providing false, distorted or tendentious information.

Main employment terms and motivation

The main terms of the CEO's employment agreement for the Board to consider are:

- Non-compete – the main function of a non-compete clause is to provide the company with greater assurance that its intellectual property, information on clients, confidential resources and proprietary information will not be made available to or used by a competitor.
- Non-solicitation – this clause assists the company in retaining valuable employees and reduces the risk of their being recruited by a former CEO who would use their knowledge for competitive advantage.
- Confidentiality – a clause that goes hand in hand with the non-compete clause and prohibits the former CEO from sharing the company's confidential information, trade secrets and know-how with any third party, in particular a competitor, after the end of employment.
- Notice period – a clause setting the period of notice to be given by the CEO to the company, or by the company to the CEO, before termination takes effect. If no notice period is agreed, the statutory period applies, which may not suit the company's needs.

Once the CEO is selected, the Board should make sure that the CEO is motivated and appropriately remunerated in line with market and industry practice, using well-established means such as performance bonuses, share options and fringe benefits (company car, health care, life insurance and similar). The motivation system aims to ensure the achievement of the company's long-term goals.

Evaluation of performance

Evaluating the performance of the CEO is the responsibility of the Board, which often asks its relevant committee for assistance. The CEO is the link between the Board and the management team in the governance of the company, and the Board has an interest in the CEO being effective. As the Board and the CEO share responsibility for ensuring that the company meets its goals and objectives, the

following aspects of preparing and running the evaluation of the CEO's performance should be considered:

- the criteria against which the review is undertaken, agreed in advance;
- the use of common methods and tools for such reviews (360° feedback, company performance, stakeholder relations);
- a process run by the Board (its Chair) or a Board committee;
- an agenda for the review and the key issues to be discussed;
- sufficient time to prepare;
- an open and transparent manner (constructive criticism, areas for improvement, acknowledgement of achievements).

The purpose and benefits of evaluating the CEO's performance include:

- aligning the CEO's capabilities with the strategic direction of the company;
- spotting any potential management problems early on;
- setting appropriate goals for future growth;
- giving the Board greater objectivity about the CEO's remuneration;
- promoting collaboration between the CEO and the Board.

The success of the CEO's evaluation depends largely on setting the right KPIs at the outset and tracking the CEO's performance against them. KPIs may be "hard", based on specific metrics and therefore easily measurable (such as adherence to budget, financial performance or employee turnover), or "soft" and more difficult to measure (such as communication and personal qualities). The most widely used KPIs are SMART: specific, measurable, achievable, relevant and time-bound. Such KPIs enable the Board to make data-driven decisions, identify areas where the CEO or the company is falling short and take swift action to improve. Companies may choose other frameworks for setting the CEO's goals and objectives, such as OKRs (objectives and key results), FAST (frequently discussed, ambitious, specific, transparent) or CLEAR (collaborative, limited, emotional, appreciable, refinable).

The CEO's performance should be monitored and constructive feedback given on an ongoing basis (quarterly or at least twice a year). This alerts the Board to emerging issues and gives the Board and the CEO the opportunity to address them before they escalate.

Succession planning

Succession planning is critical to the continuity of the business and is increasingly recognised as a significant aspect of good corporate governance. It is the process of identifying and developing new leaders and key employees who can replace

existing ones when they leave or retire. Failure to focus on succession planning may result in a weak, ineffective and insufficiently diverse senior management team, which in turn creates a risk to the company's long-term success.

The aims and advantages of good succession planning include:

- ensuring that the senior management team consists of people with the right diversity of skills and talent needed to achieve the company's business objectives and promote its long-term success;
- having a procedure for identifying and developing possible successors to the CEO and other key employees, which includes determining the experience, professional capabilities and personal characteristics needed for each senior management role and assessing candidates in the light of the company's strategy and culture; and
- selecting the optimal candidates to replace the CEO and other key employees following their departure, whether planned or unexpected.

There is no one-size-fits-all way of approaching these issues, nor is there one specific succession planning procedure that would suit every company. The Board must therefore take into account the company's particular situation when formulating and implementing its succession planning policy.

To maintain continuous and efficient operations and a seamless transition of leadership, the succession planning process should be properly defined and implemented. A written succession plan is therefore highly recommended. It should at least include:

- the key (critical) management positions in the company;
- potential successors, their development plans and development opportunities;
- a step-by-step plan for emergency succession;
- alignment with the company's strategy;
- legal and financial considerations;
- regular review and updating.

The succession plan and its execution should be reviewed by the Board at least annually.

KEY TAKEAWAYS

A. Selecting, motivating, evaluating and, when necessary, replacing the CEO is one of the Board's most important functions. The selection is best run by the nomination committee, where one exists, and the profile must match the company's stage of development and expected needs.

B. Internal and external candidates each have advantages; the Board weighs continuity and cultural fit against fresh perspective and change capability in the light of the company's long-term goals.

C. A new CEO needs structured onboarding, early and regular feedback, tolerance of initial mistakes and a Board that respects the boundary between oversight and management.

D. The CEO's contract should address non-competition, non-solicitation, confidentiality and the notice period, and the remuneration should motivate the achievement of long-term goals.

E. The Board evaluates the CEO against criteria and KPIs agreed in advance, in an open and transparent process, with feedback at least twice a year.

F. Succession planning for the CEO and other key positions, including an emergency plan, is part of good governance; the plan should be written and reviewed by the Board at least annually.

QUESTIONS FOR THE BOARD

1. *Does the Board have an agreed profile for the CEO that reflects the company's stage of development and strategy, and a defined process, led by the nomination committee or the Board, for selection and re-appointment?*
2. *How did the Board support the current CEO in the first months, and does it respect the line between oversight and management?*
3. *Does the CEO's contract contain adequate non-compete, non-solicitation, confidentiality and notice provisions, and when were they last reviewed?*
4. *Against which KPIs and criteria is the CEO evaluated, were they agreed at the start of the year, and when did the Board last give the CEO structured feedback?*
5. *Do we have a written succession plan for the CEO and other critical positions, including emergency succession, and when did the Board last review it?*
6. *Who would run the company tomorrow if the CEO were unexpectedly unavailable, and does that person know it?*

5.5.2

REMUNERATION OF THE CEO, MANAGEMENT AND EMPLOYEES

Remuneration policy

The Board is responsible for establishing the remuneration policy for the CEO, Management Board members, other managers and employees of the company and for ensuring its effectiveness. To assist the Board in this responsibility, a remuneration committee may be established; larger companies and public-interest entities usually establish one, to comply with the more stringent regulatory requirements that apply to them and with good corporate governance practice.

In relation to remuneration, the main functions of the Board are to:

1. adopt the remuneration policy and ensure its regular review;
2. oversee the implementation of the remuneration policy and practices, to make sure that the policy operates as intended and continues to comply with applicable laws;
3. ensure that the remuneration of the CEO and management, both the elements of the package and the actual amounts awarded, achieves the objectives of the remuneration policy;
4. provide sufficient information to shareholders and other stakeholders to ensure external transparency of the remuneration policy and of management remuneration packages.

For listed companies, the EU Shareholder Rights Directive II, as transposed in Estonia, Latvia and Lithuania, requires the remuneration policy to be submitted to the general meeting of shareholders for a vote and an annual remuneration report to be published and put to the general meeting. State-owned and municipally owned enterprises are subject to additional statutory rules and limits on management remuneration. The Board should know which of these requirements apply to the company.[23]

The remuneration policy, and the practices used to determine remuneration, should be clear, documented and transparent. The remuneration policy should:

1. state its objectives, which should generally be to ensure that the company:
    a. provides strong incentives for management to perform in a way that is aligned with the company's long-term goals and increases long-term value

for its shareholders and other stakeholders, taking into account the company's sustainability (ESG) goals;

   b. attracts and retains the talent necessary for its successful operation;

2. be aligned with the company's purpose, vision, mission, strategy, long-term objectives and values;
3. be objective and fair, based on rewarding performance and results aligned with the long-term goals of the company;
4. be gender-neutral, non-discriminatory and inclusive;
5. provide an effective framework for performance measurement and a clear link between reward and performance aligned with the company's long-term goals;
6. include the following:
   a. a description of the structure of the remuneration package, listing all components of fixed and variable remuneration, including all bonuses and other benefits in whatever form that may be awarded to management, and their relative proportions;
   b. a link between the variable part of remuneration and the financial and non-financial performance of the company and of the individual manager;
   c. where the company awards share-based remuneration, the vesting and delivery periods and, where applicable, the rules for retaining shares after delivery;
   d. the possibility of, and conditions for, adjusting variable remuneration before it is awarded (malus) and reclaiming it after payment (claw-back), in the event of failure to achieve the performance targets, payment based on misstated data or serious misconduct by the manager concerned;
   e. the deferral of part of the cash or share-based variable remuneration;
7. be reviewed regularly, preferably at least once a year and whenever the need arises (for example, changes in the company's strategy or in labour market trends).

Management remuneration package

The management remuneration package is the total amount a manager earns for their performance and for achieving the objectives set by the Board. It may consist of various elements and usually includes:

– ***Fixed remuneration*** *(fixed monthly salary)* is non-discretionary: it cannot be unilaterally adjusted by the company or the Board and does not depend on the

23 Directive (EU) 2017/828 amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement (Shareholder Rights Directive II), Articles 9a and 9b.

manager's performance. Its amount may vary greatly according to the business sector, the manager's experience and track record and other considerations.

- ***Performance-based variable remuneration*** depends on the performance of the company and of the manager, that is, on the achievement of company and individual goals. It is good practice to ensure that such remuneration is at all times aligned with the achievement of the company's long-term goals and the shareholders' interests.

It is common to provide variable remuneration as an ***annual*** cash bonus (***short-term incentive***, ***STI***), which usually ranges from one to six months of the manager's fixed salary. Good practice, however, is for the major part of variable remuneration to be tied to the achievement of ***long-term*** goals (long-term incentive, ***LTI***). An LTI programme usually (a) runs for three to five years, (b) is larger than the STI, (c) preferably consists of shares as well as cash, (d) includes the deferral of part of the cash element, the delivery of awarded shares at the end of the programme and a requirement to retain part of the delivered shares for a certain period, and (e) allows the awarded cash or shares to be adjusted or reclaimed in the event of misconduct or a subsequent restatement of the company's financial results. The Board may also award ***a one-off*** cash bonus for extraordinary performance, significantly above the goals set or in extraordinary situations that were not taken into account when the goals were set.

- ***Other cash and in-kind benefits*** provided by the company, such as health insurance, life insurance, a car or travel allowance, pension plans, sports and wellness programmes, family leave, compensation of relocation costs and discounts on company products or services.
- ***Severance pay*** is a payment for early termination of the contract (before the end of the term for fixed-term contracts, or before retirement for indefinite contracts), which may amount to 6 to 18 months of fixed monthly salary. Such conditions could be a subject to national law.

When defining and reviewing the management remuneration package, the Board should take into account the latest market data and trends in salaries, to ensure that its decision fits the market and motivates management.

KEY TAKEAWAYS

A. The Board establishes the remuneration policy for the CEO, management and employees and ensures its effectiveness, usually with the support of a remuneration committee in larger companies and public-interest entities.

B. The policy should be clear, documented and transparent, aligned with the company's purpose, strategy and values, objective, fair and inclusive, and built on a clear link between reward and performance against the long-term goals, including sustainability goals.

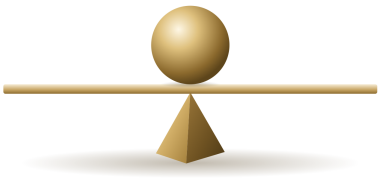
C. The policy should describe all components of fixed and variable remuneration and their proportions, link variable pay to financial and non-financial performance, and provide for deferral, share retention, malus and claw-back.

D. A remuneration package typically consists of fixed salary, short-term and long-term variable remuneration, other benefits and severance terms; good practice ties the larger part of variable pay to long-term goals through an LTI programme of three to five years.

E. For listed companies the remuneration policy and report are put to the shareholders under SRD II, and state-owned enterprises face statutory limits; the Board sets pay with reference to current market data.

QUESTIONS FOR THE BOARD

1. *Has the Board approved a remuneration policy covering the CEO, management and employees, and when was it last reviewed?*
2. *Is the variable remuneration of the CEO and management clearly linked to the company's long-term goals, including sustainability goals, and is the larger part of it long-term?*
3. *Does the policy provide for deferral, share retention, malus and claw-back, and have these provisions ever been applied?*
4. *How does management remuneration compare with the market and with the pay of the wider workforce, and can the Board justify the differences?*
5. *Are the legal requirements on shareholder approval and disclosure of remuneration (SRD II, rules for state-owned enterprises) met, and is the remuneration report clear to shareholders?*
6. *Are the amounts of severance pay in management contracts reasonable, and are they known to the Board before a termination decision is taken?*



CHAPTER

5.6

SHAREHOLDERS, STAKEHOLDERS AND ACCOUNTABILITY

How the Board protects shareholder rights, builds relationships with stakeholders and accounts for its decisions through disclosure and communication.

IN THIS SECTION

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5.6.1

RIGHTS AND EQUITABLE TREATMENT OF SHAREHOLDERS

The **protection** of shareholder rights and the **equitable treatment** of shareholders are **core elements of a sound corporate governance framework**. They are especially important in the Baltic states, where companies may have concentrated ownership structures, controlling shareholders, family owners, state or municipal owners, and, in listed companies, minority investors. Good governance requires that all shareholders are treated fairly, that their rights are respected in practice, and that control is exercised responsibly.

Shareholders **should have secure and effective rights** to participate in fundamental corporate decisions. These include the right to vote at general meetings, elect and remove Board members, approve major changes to the company's statutes or share capital, receive dividends when declared, and obtain relevant information on the company. Shareholders should also have the right to receive timely notice of general meetings, review meeting materials in advance, ask questions, submit proposals where permitted by law, and vote in person, by proxy or through electronic means where available. These rights should not exist only formally; companies should organise shareholder engagement in a way that enables informed and meaningful participation.

Equitable treatment means that shareholders of the same class should be treated equally. Minority shareholders should be protected from abusive actions by controlling shareholders, management or the Board. This is particularly relevant in companies with a dominant shareholder, family-controlled companies, state-owned enterprises, municipal companies and group structures. Transactions with related parties, changes in control, share issuances, dividend decisions, asset transfers and intra-group arrangements should be handled transparently and on fair terms. The Board should ensure that such matters are properly reviewed, conflicts of interest are managed, and decisions are taken in the interests of the company as a whole.

The Board has a **central responsibility** in protecting the integrity of shareholder governance. Board members should not see themselves as representatives of the shareholder who nominated them, but as fiduciaries of the company. Once elected, they must exercise independent judgement, act with due care and loyalty, and consider the long-term interests of the company. This is particularly important where Board members are nominated by controlling shareholders, the state, a

municipality, private equity investors or family owners. The Board should create conditions for constructive shareholder dialogue, while preserving the clear division between ownership, Board oversight and executive management.

Transparent communication is essential for shareholder confidence. Listed companies should provide accurate, timely and balanced disclosure to the market, ensuring that all investors receive material information at the same time. Private companies should also establish appropriate information flows between the company, the Board and shareholders, especially where not all shareholders are involved in management. In family businesses and closely held companies, clear reporting practices can reduce mistrust and prevent conflicts. In state-owned and municipal companies, transparency supports public accountability and helps protect the company from political or informal influence.

Shareholder engagement should be encouraged, but it should be structured and responsible: **shareholders should not bypass the Board** by giving informal instructions to management or individual Board members. The company should have clear procedures for shareholder communication, including how shareholder proposals, questions and concerns are addressed.

Equitable shareholder treatment also requires effective management of conflicts of interest. Board members, executives and controlling shareholders should disclose personal, financial or related-party interests that may affect their judgement. The company should have **clear procedures** for approving related-party transactions, including review by independent Board members or a relevant Board committee where appropriate. Material related-party transactions should be disclosed in accordance with law and good practice.

In practice, good shareholder governance depends not only on legal rights, but also on culture. **Owners should exercise their rights responsibly**; Boards should **protect the interests of the company** as a whole; and management should operate within clear authority delegated by the Board. The objective is not to weaken ownership influence, but to ensure that ownership is exercised transparently, fairly and in a manner that supports sustainable success, investor confidence and long-term value creation.

KEY TAKEAWAYS

A. The protection of shareholder rights and the equitable treatment of shareholders are core elements of governance, and especially important in the Baltic states, where ownership is often concentrated in controlling, family, state or municipal hands alongside minority investors.

B. Shareholders should have effective rights to participate in fundamental decisions: to be notified of and vote at general meetings, elect and remove Board members, approve changes to the statutes and capital, receive dividends and obtain information, in person, by proxy or electronically.

C. Shareholders of the same class are treated equally, and minority shareholders are protected from abuse in related party transactions, changes of control, share issues, dividends, asset transfers and intra-group arrangements.

D. Board members are fiduciaries of the company, not representatives of the shareholder who nominated them; they exercise independent judgement and act in the long-term interests of the company as a whole.

E. Transparent communication, structured shareholder engagement that does not bypass the Board, and the management of conflicts of interest sustain shareholder confidence; ultimately, good shareholder governance depends on culture as much as on legal rights.

QUESTIONS FOR THE BOARD

1. *Are our shareholders, including minority shareholders, able to exercise their rights effectively: timely notice, access to materials, questions, proposals and voting by proxy or electronic means?*
2. *How does the Board ensure that related party transactions, capital changes, dividends and intra-group arrangements are reviewed independently and concluded on fair terms?*
3. *Do Board members nominated by a controlling shareholder, the state or a municipality act as fiduciaries of the company, and how would the Board respond to informal instructions from an owner?*
4. *Do all shareholders receive material information at the same time, and do we have clear procedures for handling shareholder questions, proposals and concerns?*
5. *How does the Board maintain a constructive dialogue with the owners while preserving the division between ownership, Board oversight and executive management?*

5.6.2

STAKEHOLDER RELATIONSHIP GOVERNANCE

Stakeholders are individuals, groups or organisations that have a stake in the company, through interest, influence or both, each with their own needs and expectations. They range from shareholders, employees and Board members to lenders, customers, suppliers, government and local communities.

According to the G20/OECD Principles of Corporate Governance, "The corporate governance framework should consider the rights, roles and interests of stakeholders and encourage active co-operation between companies, shareholders and stakeholders in creating value, quality jobs, and sustainable and resilient companies."[24]

There are many benefits to building and maintaining positive stakeholder relationships, including:

- lower operational and project risk;
- a stronger reputation;
- buy-in for the company's plans;
- compliance with regulatory requirements;
- competitive advantage.

Identification of stakeholders

The first step is to identify the key stakeholders: to determine the stakeholder groups and understand their needs and the roles they play. Some simply need to be kept informed, while others directly influence the company's operations or the outcome of particular projects.

Mapping the stakeholders

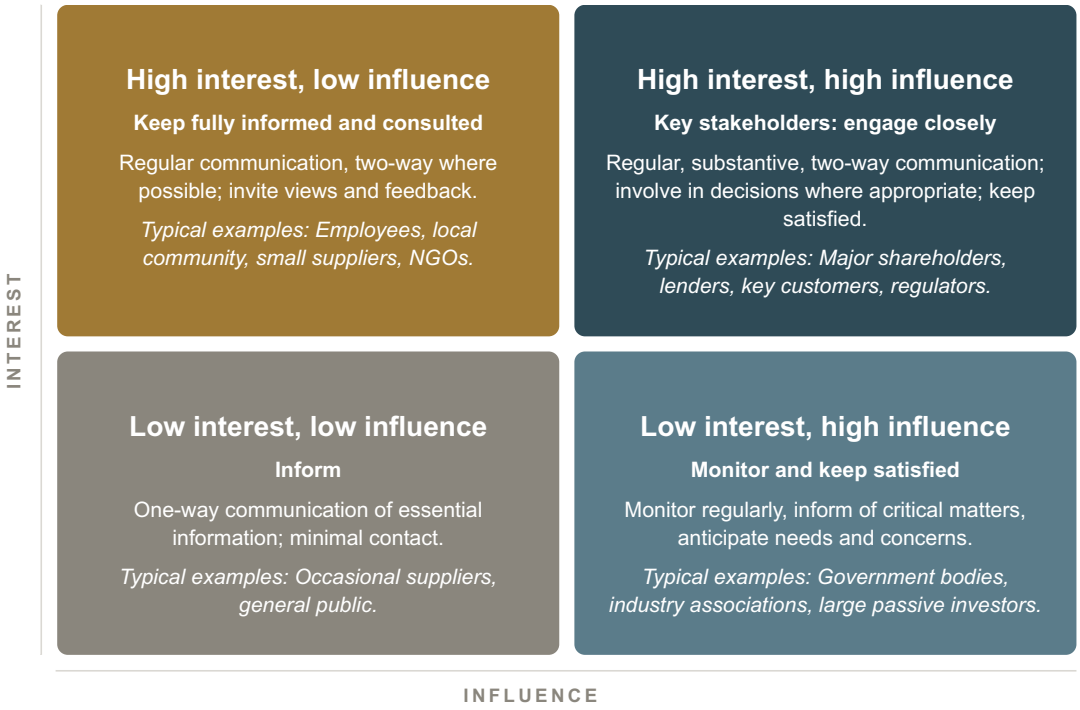
By mapping its stakeholder groups, the company can develop a plan to engage with each group in the way that works best for it. This makes the best use of resources: groups that need less attention are not over-communicated with, while the groups with high interest and high influence are engaged in greater depth.

When mapping stakeholders, place them in one of the four categories shown in the figure below.

24 OECD (2023), G20/OECD Principles of Corporate Governance, OECD Publishing, Paris, Chapter IV, The role of stakeholders in corporate governance.

Figure 5.7 **Stakeholder mapping by interest and influence**

Figure 5.7 **Stakeholder mapping by interest and influence**



Stakeholder mapping places each stakeholder group according to its interest in the company and its influence over it, so that the company can engage with each group in the way that suits it and make the best use of its resources. The key stakeholders, with high interest and high influence, are engaged closely and may be involved in decisions; highly interested groups with less influence are kept fully informed and consulted; influential groups with little day-to-day interest are monitored and their needs anticipated; and groups with low interest and low influence receive essential information only. The map should be reviewed regularly, since interest and influence change with circumstances.

It is very important to share information with stakeholders clearly and in good time, using the channels each stakeholder group prefers. Trust is established and maintained by being transparent about the status and plans of the company's activities and projects. Good communication is essential to share the company's vision with its stakeholder groups: provide the big picture, with timelines and key milestones where needed.

Another part of communication with stakeholders is active listening, one of the most important stakeholder communication skills. Listen to their feedback and make sure that their perspectives, suggestions and concerns are understood. It is good practice to convene stakeholder forums and invite key stakeholder representatives. Stakeholders who feel heard are far more likely to trust the company.

To embed stakeholder engagement in the company's operations, the Board should:

1. define stakeholder engagement as a core value;
2. identify, discuss and prioritise the key risks associated with changing societal expectations;
3. determine the Board's financial and non-financial information needs for decision-making, management oversight and the monitoring of key stakeholder relationships;
4. discuss and approve key performance indicators for social, environmental and financial performance;
5. approve a policy for external reporting;
6. integrate stakeholder issues into the annual general meeting of shareholders;
7. discuss the risks and impacts of projects and operations and provide transparent disclosure to shareholders and other key stakeholder groups;
8. convene stakeholder forums and invite key stakeholder representatives to address Board meetings;
9. consider establishing a stakeholder relations committee.

Balancing the interests of the stakeholder groups

Different stakeholder groups may have different and sometimes opposing interests. For instance, employees want higher pay while customers want lower prices, and one part of a community wants well-paid jobs while another does not want a factory built nearby.

The Board should consider the interests of the relevant stakeholder groups and find the most suitable way to balance them, taking into account the interests and long-term goals of the company.

Addressing conflicting interests requires careful consideration, compromise and effective communication by the Board, to find solutions that balance the needs of stakeholders while maintaining the sustainable development of the company and observing ethical standards. The key activities and considerations are:

1. Stakeholder identification. The Board should ensure that the company identifies its stakeholder groups and their interests (see stakeholder mapping above).
2. Stakeholder communication. The Board should ensure that the company establishes clear and consistent communication channels and delivers relevant and timely information about its activities and plans and their impact. The company should also actively seek stakeholders' feedback: communication should flow in both directions.

3. Balancing interests. Not all stakeholder groups have the same interests, so compromises are needed. The company should balance the different interests and seek solutions that benefit all sides, cooperating with key stakeholders and involving them in decision-making where appropriate. Engaging them builds a sense of mutual benefit and loyalty. The costs, benefits and risks of each alternative should be considered, together with the short- and long-term implications for the company and its stakeholders. Such an approach benefits the company's competitiveness and image.
4. Monitoring and assessment. It is important to monitor and regularly assess the results of business decisions against the interests and opinions of the stakeholder groups, for example by evaluating stakeholders' reactions and satisfaction. In this way the Board and the company understand the real consequences of their decisions and can make the necessary adjustments and improve their decision-making.

KEY TAKEAWAYS

A. Stakeholders are all those with a stake in the company through interest, influence or both; the G20/OECD Principles call for their rights, roles and interests to be recognised and for active cooperation in creating value.

B. Good stakeholder relationships lower risk, strengthen reputation, secure buy-in, support compliance and create competitive advantage.

C. Stakeholders are identified and mapped by interest and influence; the key stakeholders, with high interest and high influence, receive regular, substantive, two-way communication, while other groups are informed or monitored proportionately.

D. Communication with stakeholders is clear, timely and delivered through the channels each group prefers, and it includes active listening, for example through stakeholder forums.

E. The Board embeds stakeholder engagement in the company's operations, sets KPIs for social, environmental and financial performance, approves the external reporting policy and, where interests conflict, balances them in the long-term interest of the company and monitors the results.

QUESTIONS FOR THE BOARD

1. *Who are our key stakeholders, when did we last map them by interest and influence, and does the map reflect changes in our business and environment?*
2. *Does each key stakeholder group receive the communication it needs, through the channels it prefers, and how do we listen to what they tell us?*
3. *Which stakeholder interests conflict with each other or with the company's plans, and how has the Board balanced them in recent decisions?*
4. *Has the Board approved KPIs for social, environmental and financial performance and a policy for external reporting, and does it review them?*
5. *Do we monitor stakeholders' reactions to our decisions and adjust where necessary, and would the Board know if a key relationship were deteriorating?*

5.6.3

BOARD ACCOUNTABILITY, DISCLOSURE AND COMMUNICATION

The G20/OECD Principles of Corporate Governance state that "The corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, sustainability, ownership, and governance of the company."[25]

Timely and proper accountability strengthens the company's transparency, which improves its relationships with stakeholders and increases trust.

The Board is responsible for overseeing the company's performance, ensuring effective control of operations and being accountable to shareholders and other stakeholders for the company's activities, disclosing a true, timely and understandable picture of the company's position and prospects.

The annual report is the primary document for which the Board is accountable; it is described in the section "Disclosure and communication" below.

To give the Board, shareholders and other stakeholders external and objective assurance that the financial statements present fairly, in all material respects, the financial position and performance of the company, the financial statements must be audited by an independent, competent and qualified auditor in accordance with high-quality international auditing standards (see sub-chapter 5.2.6).

The G20/OECD Principles of Corporate Governance stipulate that the following information should be disclosed:[26]

1. The financial and operating results of the company
2. Company objectives and non-financial sustainability information
3. Capital structures, group structures and their control arrangements
4. Major share ownership, including beneficial owners, and voting rights
5. Remuneration of members of the Board and key executives
6. Information about Board members, including their qualifications, the selection process, their composition, other company directorships and whether they are regarded as independent by the Board
7. Related party transactions

25 OECD (2023), G20/OECD Principles of Corporate Governance, Chapter V, Disclosure and transparency.
26 OECD (2023), G20/OECD Principles of Corporate Governance, Principle V.A.

8. Foreseeable risk factors
9. Governance structures and policies, including the extent of compliance with the applicable corporate governance code and how it is implemented
10. Debt contracts, including the risk of non-compliance with covenants

To improve the quality of corporate disclosures, companies should move away from generic, declaratory statements in favour of **concise, company-specific reporting** that explicitly links initiatives to the company's purpose, strategy and values. This is best achieved by highlighting **measurable outcomes and impacts** rather than merely describing policies, while ensuring that all reporting on stakeholder engagement demonstrates how external views have directly influenced Board decisions. Furthermore, disclosures must provide transparency into **governance practices**, specifically detailing how the Board reviews the effectiveness of risk management systems and how executive remuneration is aligned with long-term cultural and strategic goals.

As the risk profile of the business changes constantly, accountability needs to be ingrained in the culture of the company and subject to regular review. A strong sense of accountability and the application of best practice help to safeguard the reputation of the company and of its Board members. Stakeholders scrutinise companies and their Boards ever more closely, and accountability procedures should be an important part of the Board's duties.

All relevant regulations and EU directives, in particular the Corporate Sustainability Reporting Directive (CSRD) and the accounting and transparency rules, should be taken into account when setting up the framework for the company's disclosures and reporting.[27]

The Board must ensure that all material information is disclosed in a timely manner and through the channels most suitable for the company's stakeholders.

Disclosure and communication

The significance of a company's disclosure and communication cannot be overstated: transparency fosters trust and is a crucial component of sound business practice.

Each stakeholder group has distinct interests in the company. For instance:

– shareholders and investors are interested in the company's performance, prospects, governance practices and Board composition;

27 Directive (EU) 2022/2464 on corporate sustainability reporting (CSRD); its scope and timetable were amended by the EU "Omnibus" simplification package adopted in 2025–2026.

- regulators and authorities are concerned with the company's compliance with laws and regulations;
- customers focus on the safety and sustainability of products and on warranties;
- employees are interested in the company's performance, remuneration practices and workplace safety.

Further details on stakeholder groups and their interests can be found in sub-chapter 5.6.2.

The Board should ensure that the **communication strategy** is grounded in stakeholder mapping and prioritisation. In this way the Board helps the company to build robust relationships with its stakeholders, manage risks more effectively and achieve its objectives, with better outcomes for all parties.

The Board should formulate and approve a **disclosure and communication policy** that sets out how the company communicates and discloses information and how the Board oversees this. All other internal documents on the subject should be developed on the basis of this policy and approved by the CEO. The information disseminated by the company should be timely, accurate and relevant.

The primary sources of disclosure and communication are the following.

The **company's annual** report is a fundamental document of its accountability, and the Board should be actively involved in its preparation. A well-crafted annual report should be comprehensible to a broad audience, not only to experts. Besides information about the company's past performance and current position, it should include the latest developments and a view of the future. The annual report should contain the following key sections:

- letters from the Chair of the Board and the CEO;
- the company's purpose, vision, mission and values;
- brief highlights of the strategy (the full strategy document should remain confidential);
- the major risks that could prevent the company from achieving its objectives, how they are managed and how risk management is organised;
- analysis of external factors and trends and of the internal situation of the company;
- a description of the company's operations, its business model and how value is created;
- the governance of the company, including the Board and its committees, their performance and remuneration, governance practices and policies and performance against them;

– the company's financial and non-financial (including sustainability) performance against the targets set.

The Board should lead the preparation of the annual report, with management preparing the information. It is good practice to divide the preparation into steps:

1. discussion and agreement of the topics (the table of contents);
2. preparation by management, and review by the Board, of the first draft of the non-financial part;
3. final review of the full document, including the financial information;
4. endorsement of the annual report and its submission for approval by the general meeting of shareholders. The annual report should be communicated both internally and externally and be accessible on the company's website.

In recent decades companies have adopted a broader form of accountability, integrated **reporting**: a process that results in communication by the company, most visibly a periodic integrated report, about how it creates value over time. The Integrated Reporting Framework is now maintained by the IFRS Foundation.[28]

The Board should be aware of recent and forthcoming **EU rules** on corporate reporting, in particular the CSRD, the European Sustainability Reporting Standards (ESRS) and the Corporate Sustainability Due Diligence Directive (CSDDD), and ensure that the company complies with them.

The **company's website** is another vital, easily accessible and widely used source of information. It should be user-friendly, allowing easy navigation and access to up-to-date and relevant information, and offer interactive communication.

The website should contain comprehensive information about the major owners, the Board, management and the internal auditor. All relevant documents, such as the articles of association, the charters of the Board and its committees, policies, codes and annual reports, should be readily accessible.

If the company operates beyond its country of registration, it should provide information in other languages, ensuring that the scope of information is consistent across all languages. A whistleblowing section (see sub-chapter 5.3.3) should be prominently placed on the home page for easy access. Given the risk of hacking, robust security measures and regular back-ups of the website are essential.

To ensure effective corporate communication, the Board must take a proactive approach to overseeing communication practices, processes and monitoring mechanisms. This helps to safeguard and enhance the company's reputation, foster

28 IFRS Foundation, Integrated Reporting Framework (2021), available at www.integratedreporting.ifrs.org.

stakeholder trust and promote the company's success. To this end, the Board should:

1. approve a comprehensive communication strategy;
2. formulate and approve a disclosure and communication policy;
3. ensure that a dedicated person, such as a communication manager, is responsible for corporate communication;
4. regularly assess the CEO's communication;
5. regularly review and approve key communication materials, such as the financial statements and the annual report;
6. ensure that a crisis communication plan is in place, regularly reviewed and updated and supported by training (see sub-chapter 5.2.4);
7. ensure effective internal communication.

The primary communicator should be the CEO, with the Chair or other Board members stepping in only when the CEO is unable to communicate, for instance because of misconduct or absence.

The Board must remember that it is the ultimate guardian of the company's reputation.

Reputation management

In creating and maintaining reputation, the Board's role is to ensure that all the factors contributing to the company's reputation are coordinated, including the reward and incentive systems. If these systems reward individual action, communication about teamwork will be ineffective, since people behave in line with how they are measured rather than with what they are told.

With **social networks**, customer service has become part of public communication, since customers often express their dissatisfaction on these platforms. The Board must therefore ensure that customer service systems and standards are aligned with the communication strategy and that practical solutions are implemented when issues become public.

KEY TAKEAWAYS

A. The Board is accountable to shareholders and other stakeholders for the company's activities and must ensure timely, accurate and understandable disclosure of all material matters, as the G20/OECD Principles require.

B. The annual report is the primary document of accountability: the Board decides its structure, reviews the non-financial part, endorses the final report for approval by the general meeting and ensures its publication; the financial statements are audited by an independent auditor.

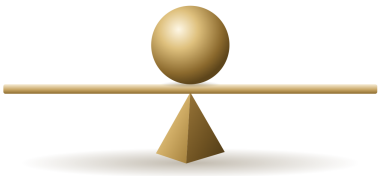
C. Disclosure should be concise and company-specific, linking initiatives to purpose, strategy and values, showing measurable outcomes and explaining how stakeholder views have influenced Board decisions, in compliance with EU reporting rules such as the CSRD and ESRS.

D. The Board approves a disclosure and communication policy and a communication strategy grounded in stakeholder mapping, ensures a dedicated communication function, reviews key materials, and keeps a crisis communication plan ready; the CEO is the primary communicator.

E. The company's website is a vital source of information, with up-to-date documents, information in the relevant languages, a prominent whistleblowing section and robust security; the Board is the ultimate guardian of the company's reputation, including in customer service and social media.

QUESTIONS FOR THE BOARD

1. *Does the Board decide the structure of the annual report, review the non-financial part and endorse the final document before it goes to the general meeting?*
2. *Is our disclosure company-specific and outcome-focused rather than generic, and does it show how stakeholder views have influenced the Board's decisions?*
3. *Do we comply with the reporting requirements that apply to us, including the CSRD and ESRS where in scope, and who verifies this?*
4. *Has the Board approved a disclosure and communication policy and a communication strategy, and who is responsible for corporate communication?*
5. *Is the company's website current, complete and secure, with the key governance documents and a whistleblowing channel easily found?*
6. *Is a crisis communication plan in place and tested, and does the Board know when it would be expected to step in for the CEO as communicator?*



CHAPTER

6

BOARD WORK ORGANISATION

How to organise Board work in practice: planning, meetings, decision-making, committees, the Board secretary and regular evaluation.

IN THIS CHAPTER

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6.1

EFFECTIVE BOARD WORK: PLANNING, MEETINGS, MATERIALS AND MINUTES

Leading by example starts at Board level: an effectively organised Board translates into smooth processes throughout the company, from aligned decision-making cycles and calendars to well-defined internal governance processes, policies and documents.

The Board should set its overall objectives for the term of its appointment, aligned with the shareholders' letter of expectations, and translate them into annual goals and deliverables. It is good practice to review the objectives annually.

Planning of Board work

It is recommended to plan the annual Board work to cover both routine tasks (compliance reports, regular approvals) and strategic focus areas. The mix of agenda items should reflect all key areas of the Board's responsibility. A deep dive into a particular business area can lead to better understanding, involvement and strategic input or risk mitigation, and guest speakers such as key suppliers, customers or market experts can contribute to value creation and shared know-how. The annual plan (*see the examples of an annual plan and a Board calendar in Annex 5*) can be converted into an annual Board calendar with preliminary agendas for Board meetings and other events (strategy session, Board self-evaluation and similar). It should be communicated internally, so that everyone knows what has to be prepared and submitted to the Board and when, and it should be integrated into the company's decision-making processes and, where applicable, its external reporting requirements.

Board meeting agenda

The Board should put more emphasis on the future and on strategic issues than on the past and operational issues (the 80/20 rule). Important decisions, including strategic ones, should be taken in the first part of the meeting, with management reports and items for information following. Past and operational issues should be addressed by the Board mainly where they fall outside the normal or expected range, in which case they usually involve risk or compliance.

The meeting agenda should be prepared by the Chair in consultation with the CEO and with the assistance of the Board secretary, on the basis of the annual Board work plan, the preliminary agendas and current items. The draft agenda is distributed to Board members for feedback and suggestions; the final version is

then distributed by the Board secretary to all Board members and to the CEO or Management Board. The CEO allocates the agenda items and related tasks to those who will prepare the materials for the meeting.

It is not good practice to add new agenda items during the Board meeting, because no materials are available and the discussion will be ineffective. Exceptions may be made for urgent and important matters if all Board members agree.

Recommended structure of Board meeting agenda

1. appointment of the secretary of the meeting (if there is no permanent secretary);
2. declaration of conflicts of interest by each Board member in respect of the topics of the meeting (if any);
3. approval of the agenda (including any changes);
4. management report, covering all relevant developments since the last Board meeting;
5. oversight of strategy implementation;
6. strategic topics (achievement of strategic goals, strategic projects);
7. topics for decision (budget, investments, policies, procedures, agreements), including the preliminary wording of all proposed decisions; for the most important proposals it is good practice to have a Board submission (cover) letter, memo or similar formal document signed by the responsible persons (CEO, CFO, chief legal officer, chief compliance officer);
8. reporting (Board committee reports, financial and non-financial reports, projects, programmes, risks, compliance, internal audit, implementation of Board decisions);
9. other topics;
10. Board meeting evaluation and other Board-only topics (without management);
11. the Chair's feedback to the CEO on the Board meeting.

To make the agenda as clear as possible to all participants and to those preparing the materials, the agenda should indicate:

- the start and end time of each topic (for example 09:45–10:15), so that every participant (Board members, employees, invited guests) knows when it begins and ends;
- whether each topic is for decision, for information or for discussion;
- who will present each topic (not only the CEO or CFO, but also heads of departments); it is good practice to invite the responsible employees to present

their topics and answer the Board's questions, so that they feel more engaged and receive the Board's feedback directly;

- how much time is allocated to the presentation of each topic (5 to 10 minutes is recommended, since all Board members have read the materials and there is no need to go through them again), so that the presenter knows how much time is available;
- how much time is planned for the Board's discussion of each topic, depending on how new and challenging it is.

A clearly defined agenda contributes to the efficiency of the whole meeting by helping all participants keep to the timing of presentations and discussions.

From time to time the Board may take a deep dive into a specific topic or area to discuss opportunities or to gain a better understanding of a particular subject or environment. Depending on the subject, the Board decides whether the session is formal (part of the meeting agenda) or informal.

It is good practice to hold a short feedback session among Board members only, immediately after the formal meeting, on what went well and what can be improved. The Chair then communicates any recommendations for improvement to the CEO.

If a Board meeting is planned to run for more than two hours, a short break approximately every one and a half hours is recommended.

A strong recommendation: no surprises for the Board, neither bad nor good.

Board meeting materials

Board meeting materials should be prepared for decision-making, distilling the essence of the recommended decision and its alternatives, with supplementary materials as annexes. All materials to be presented during the meeting should be included in the Board pack. Every Board should discuss and agree with management the appropriate depth, volume and scope of the regular reports.

The materials should be prepared and delivered to the members in advance (at least seven calendar days is advisable), and Board members may send important clarifying questions to management in advance so that answers can be prepared in time.

The success of the Board meeting depends very much on the quality of the materials.

A good set of Board materials helps to achieve:

- high quality of the Board decisions based on relevant and timely information;

– effective Board work, with decisions adopted in a constructive way and without unnecessary delay.

Board meeting materials are a formal record of the Board's decision-making process, and management has a responsibility to flag problems and opportunities clearly and simply (see the business judgement rule in sub-chapter 8.1).

Each item that requires a decision should be accompanied by a structured Board submission letter (*see Annex 6*).

Checklist for the preparation of Board materials and Board submission letters:

Legal and fiduciary responsibilities	Does the Board have the authority to make the decision? Is the decision in line with legal requirements? Is the proposal in the best interests of the company? Does anyone have any conflict of interest? If the proposal is contentious, does it include more than one source of advice?
Complete	Is there enough information, analysis, supporting facts for the Board to make an informed decision with confidence?
Relevant	Is all the information relevant or does it include "nice to know" and unnecessary information?
Accurate	Are the numbers and facts accurate? Is there a clear distinction between facts and opinions?
Strategy	Does the information provided comply with the company's strategy and the best long-term interests?
Sustainability (ESG)	Do the information provided and the proposals made align with the company's sustainability (ESG) goals and initiatives?
Financial assessment	What effect will the proposal have on the financial situation or forecasts, and is it within the approved budget?
Risks and compliance	Does the proposal include the identification, assessment and mitigation of risks? Are there compliance related issues and how are they addressed?
Implementation	Does the implementation of the decision require changes to any internal governance or operational documents, such as policies, procedures or management plans? Does the proposal include monitoring and measurement arrangements? What communication is needed with stakeholders?
Standard form (template)	Does each Board submission letter follow the standard structure?

Typical problems with Board meeting materials:

– written for management, not for the Board: a great deal of unnecessary and irrelevant information about operational issues that can distract the Board from its governance role;

- assumptions of shared knowledge: the Board usually does not have the same depth of understanding of a topic as management, so acronyms and jargon may not be understood;
- “selling” a decision, which can create a false sense of security about the company’s position;
- no decision proposed or formulated, and no arguments provided;
- no alternatives presented and no pros and cons;
- poorly written and structured: the Board expects to see the key messages spelt out simply and clearly, not essays with an introduction, body and conclusion;
- poor layout: a bad first impression may influence the Board’s attitude to the content, and a document with long paragraphs, lengthy bullet lists and too much information squeezed into a tight space is difficult to read.

Running an effective Board meeting

The outcome of a Board meeting depends very much on the preparation of each Board member and each participant. The key role in ensuring the effectiveness of the meeting lies with the Chair of the Board (who usually chairs the meeting), supported by the Board secretary. The Chair is responsible for leading the meeting but is not the “boss” of the Board members and should behave accordingly.

Every Board member and invited participant arrives in good time so that the meeting can start on time. Seating should be arranged so that each Board member can see and hear the others. The CEO and the Board secretary should sit on either side of the Chair, who usually needs to communicate with both of them during the meeting.

A thorough and constructive discussion, conducted in good faith and aiming at consensus, is recommended. Frequent disagreement may indicate internal tensions in the Board or the company.

The Chair should organise the discussion of each item so that every member has a say and equal time to express their views. It is recommended that the Chair gives the floor to each member in turn and, after all have spoken (asked questions, made suggestions, put arguments), expresses their own opinion and summarises the discussion.

During the meeting the Chair summarises the discussion of each item, any assignments and the decisions, for recording in the minutes. The Chair must ensure that the timing set in the agenda for each item is kept, so discussions should be short and clear, avoiding unnecessary chatter. The discussion is first of all among Board members; other participants speak only when asked.

Minutes of the Board meeting

The minutes are ultimately the only document that can explain why and how the Board took a decision and that it was taken in the best interests of the company. The record of the discussion, questions, answers and arguments should show that the Board acted in good faith and with due care, for a proper purpose and in the absence of a material personal interest, and reached a rational decision that was reasonable for each member to reach.

To ensure a proper record, the Chair should state the decision very clearly (especially if it differs from the prepared draft) and the votes of the Board members. The key points of opinions and arguments are normally recorded, and a Board member may specifically state that a view is expressed “for the minutes”.

The minutes are a record of the Board’s decisions and of the process by which they were made. They should list the main arguments of the Board members in favour of the decision and the reasons why alternatives were not adopted. Minutes are neither a transcript of the discussion nor merely a list of decisions: they should clearly show how the Board came to a specific decision. Any independent advice received on any aspect of the discussion should be recorded, and particular attention should be paid to recording strategic and risk-related matters.

The draft minutes should be prepared and distributed to Board members, for example as a shared file accessible to all, within two to three working days, and Board members should respond with any comments within three working days, failing which they are deemed to have approved them.

It is advisable for the minutes to be signed by the secretary and all Board members.

The procedure for preparing and approving the minutes should be described in the Board charter.

Common shortcomings in minutes:

- failure to document the quorum throughout the meeting;
- poor and unclear description of Board decisions, actions and statements;
- lack of the reasons and arguments for which a decision was adopted;
- long delay in providing the draft minutes after the meeting (good practice: two to three working days);
- long delay in collecting the Board’s comments and providing the final version (good practice: two to three working days).

KEY TAKEAWAYS

A. Effective Board work starts with planning: objectives for the term aligned with the shareholders' expectations, an annual work plan covering routine and strategic items, and an annual calendar communicated throughout the company.

B. The agenda gives priority to the future and to strategy (the 80/20 rule), places decisions before reports, and shows for each item whether it is for decision or information, who presents it and how much time is allocated. New items are not added during the meeting except in urgent cases with everyone's agreement.

C. Board materials are prepared for decision-making, delivered at least seven days in advance and accompanied by a structured submission letter for each decision; management must flag problems and opportunities clearly, and the Board agrees with management the depth and scope of regular reports.

D. The Chair runs the meeting so that every member has a say and equal time, keeps to the agenda, summarises the discussion and the decisions, and speaks last; a short Board-only feedback session follows each meeting.

E. The minutes are the only record of why and how the Board decided: they capture the arguments, the alternatives rejected, any independent advice and the votes, are circulated within two to three working days and are signed by the secretary and the Board members.

QUESTIONS FOR THE BOARD

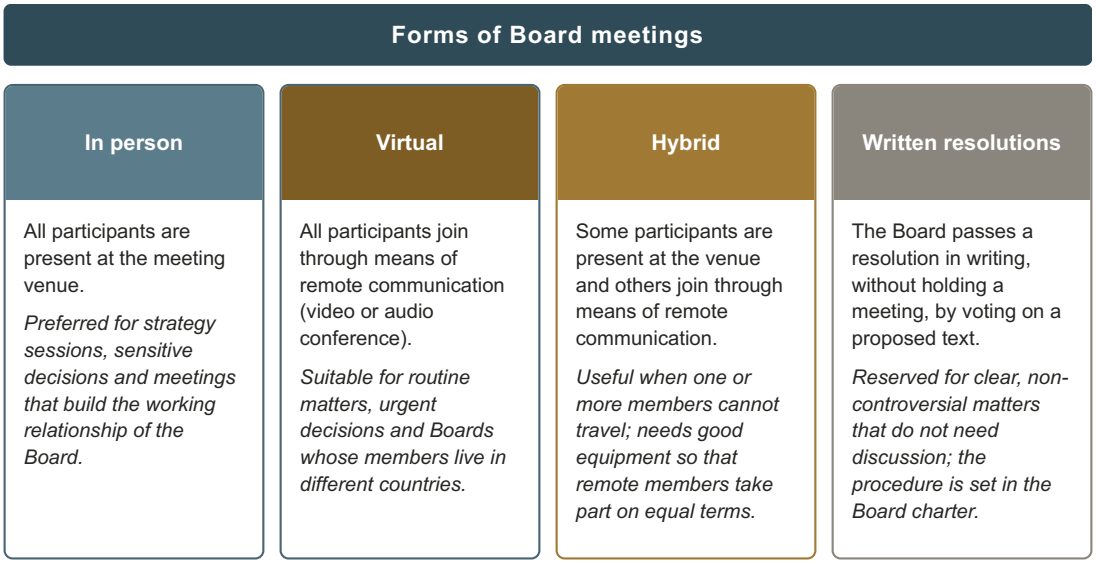
1. *Does the Board have agreed objectives for its term and an annual work plan and calendar, and does the agenda mix reflect all key areas of its responsibility?*
2. *How much of the last meeting was spent on the future and strategy, and how much on the past and operations?*
3. *Are the materials delivered at least seven days in advance, written for the Board rather than for management, and accompanied by a submission letter with a proposed decision, alternatives and risks?*
4. *Does every Board member speak on every significant item, and does the Chair summarise the discussion and the decision before moving on?*
5. *Would our minutes allow a reader in three years' time to understand why the Board decided as it did, and are they circulated and approved within the agreed deadlines?*
6. *When did the Board last hold a Board-only feedback session after a meeting, and what changed as a result?*

6.2

FORMS OF THE BOARD MEETINGS

The Board may hold meetings in person, virtually by telephone or video conference or by comparable means of remote communication, or in a hybrid format combining in-person and remote participation. In exceptional cases the Board may pass resolutions in writing. The Board charter should set out the forms of Board meeting used in the company and the organisational arrangements for each, including the submission of documents and the decision-making procedure.

Figure 6.1 **Forms of Board meetings**



Choosing between in-person, virtual and hybrid meetings

In practice, in-person meetings remain the best format for Board meetings: they allow direct and immediate communication, non-verbal cues can be observed, and the informal contact before, during and after the meeting builds the personal connections and trust on which teamwork and decision-making depend. Moving away from them should not be decided without careful evaluation.

There is, however, no one-size-fits-all approach. Some Boards need in-person meetings because of the nature of their work, non-routine issues or the need for stronger personal connections; others, especially those with geographically dispersed members or time constraints, benefit from virtual meetings, which eliminate travel time and costs, are easier to schedule and increase attendance. A hybrid approach may offer the best of both: personal contact when necessary and the efficiency of virtual meetings for routine matters. Each company should weigh its objectives, costs and the concerns of its Board in choosing the format.

Whatever the format, remote members must have the same opportunity to participate as those in the room, and it is easy to attend a virtual meeting without paying full attention. Companies introducing virtual or hybrid meetings should therefore ensure that they have a secure system providing multi-party audio, the transfer of documents and voting, and, for hybrid meetings, a process that gives equal opportunities to in-person and remote participants.

When deciding on the form of a particular meeting, the Board should also consider its agenda, for example:

- whether the meeting is limited to routine issues or includes non-routine ones;
- whether significant business transactions or governance, operational or performance issues will be discussed;
- whether a virtual or hybrid meeting is in the interests of the majority of Board members;
- whether meaningful engagement among Board members is possible.

Procedures for virtual and hybrid Board meetings

The format of each meeting and the instructions for participation should be communicated clearly in advance, and the Board calendar should show the format of the meetings planned for the whole year.

Once a company has decided to hold virtual or hybrid Board meetings, it should adopt formal rules for participation in them, covering the mechanisms for participation and for voting by remote means. These rules should be integrated into the Board charter. They should regulate at least the following:

- the identification of Board members;
- measures to ensure that all Board members can participate in the meeting, including the opportunity to follow the whole discussion;
- the mechanism enabling Board members to vote during the meeting;
- the procedures for documenting or recording the meeting;
- other administrative, technical and logistical matters.

To ensure that virtual or hybrid participation provides the same opportunity for dialogue among Board members, management and other participants as an in-person meeting, Boards should follow good practices such as the following:

- take account of all members' views before choosing between a virtual, hybrid and in-person meeting, evaluate members' responses to previous virtual meetings and consider requests to hold subsequent meetings in person;

- establish a meeting protocol or guidelines explaining how the meeting will run and how its main elements will be handled (how to present, when members may speak, how to raise a virtual hand, how to ask questions);
- ensure equal access to present information and take part in discussions, especially in hybrid meetings where some members are in the room and others remote;
- assign additional roles to facilitate virtual or hybrid meetings (for example, a person responsible for monitoring the online attendees to ensure that they receive the information and get time for discussion, questions and comments);
- keep Board members engaged (cameras on, assignments to present particular items, inviting members who have not spoken to contribute, survey tools to gather opinions);
- provide Board members with the technical support they need to participate.

Written resolutions

If all members agree, the Board may take decisions in writing.

The decision, and the fact that it was taken in writing, must be recorded in minutes. The decision becomes valid when all Board members have signed the minutes, unless the Board charter provides otherwise.

The purpose of Board meetings, however, is for the Board to meet, and the larger the Board, the more likely it is that someone will want to discuss an issue before a decision is taken. For difficult issues, and in companies with many Board members, it is therefore hard to take decisions without a meeting. Written resolutions are usually used for routine or minor issues that do not require discussion, or for topics that were presented and discussed at a previous meeting but could not be decided at the time because of missing information or timing, so that the formal decision is taken afterwards in writing.

Recommendations for Board decisions taken in writing:

- all Board members must agree that the decision is taken in writing;
- the minutes must indicate that the decision was taken in writing;
- all Board members must sign the minutes;
- the date of the decision must be indicated in the minutes.

KEY TAKEAWAYS

A. Board meetings may be held in person, virtually, in hybrid form or, exceptionally, by written resolutions; the Board charter should set out the forms used and the arrangements for each, including the submission of documents and the decision-making procedure.

B. In-person meetings remain the best format for substantive discussion and for building trust; virtual and hybrid meetings bring flexibility, lower cost and higher attendance but must give remote members the same opportunity to participate.

C. The choice of format depends on the agenda: routine items suit virtual meetings, while significant transactions, governance and performance issues call for in-person discussion.

D. Virtual and hybrid meetings need formal rules integrated into the Board charter (identification, participation, voting, recording) and good practices such as a meeting protocol, equal access, a facilitator for online attendees and measures to keep members engaged.

E. Written resolutions require the agreement of all members, are recorded in minutes signed by all and dated, and are reserved for routine or minor matters or for decisions already discussed at a meeting.

QUESTIONS FOR THE BOARD

1. *Does our Board charter set out the forms of meeting we use, and the rules for participation, voting and recording in virtual and hybrid meetings?*
2. *How do we decide the format of each meeting, and is the format shown in the annual Board calendar?*
3. *Do remote participants in our hybrid meetings have the same opportunity to see the materials, take part in the discussion and vote as those in the room?*
4. *Are our systems for virtual meetings secure, and is technical support available to every Board member?*
5. *How often do we use written resolutions, and are they limited to routine matters or decisions already discussed in a meeting?*

6.3

DECISION-MAKING: DISCUSSION, REACHING A DECISION AND VOTING

Basis for Board decisions

The decision-making process is sometimes said to be more important than the decision itself, because no one can know whether the right decision has been made until the outcome is known.

Boards should base their decisions on an analysis of the facts and pay attention to following a proper process.

Questions for each Board member to consider before a decision is adopted:

1. Is the Board the right body to take this decision; is it within its competence?
2. Do I, or does any other Board member, have or potentially have a conflict of interest? If so, see sub-chapter 5.3.4.
3. What is the problem to be resolved? What is the Board trying to achieve through this decision?
4. Is it in the best interests of the company? Is the proposed decision in line with the company's long-term vision and strategy? Am I acting fairly and honestly?
5. What are the possible alternatives, advantages and disadvantages of each?
6. What are the main factors to consider for each alternative?
    a. What are the costs and benefits of each alternative?
    b. Is a risk analysis provided? How could the risks be managed?
7. Do I have, and understand, all the necessary facts and information? What are the gaps? Are the assumptions reasonable, and should they be challenged?
8. Does the Board have sufficient expertise to take this decision, or does it need additional internal or external advice?
9. Why do I consider this the best decision, and on what grounds? Can I explain it? Is it reasonable in my objective opinion?
10. What communication is necessary about the decision?
11. How will the Board monitor the implementation of the decision?

Balancing stakeholder interests. Boards face complex decisions that benefit some stakeholders while disadvantaging others. Such choices should be made in the long-term interests of the company, and Board members need to be able to explain their decisions, including how the impact on affected stakeholders has been considered and what the company plans to do in mitigation.

The role of the Chair. The Chair guides the direction and priorities of the meeting, ensures that the Board has effective decision-making processes and that major proposals are sufficiently challenged, invites the opinion of each member and speaks last.

Quality of discussion. Boards do not usually carry out their own analyses but rely on the materials presented by management; the Board is, however, entitled to obtain the opinion of external experts or other competent third parties where the complexity of the matter requires it. The decision-making process focuses on asking challenging questions and helping management to develop alternatives. The Board must avoid the trap of groupthink, which arises when a Board falls into the habit of rubber-stamping decisions and avoiding diversity of thought, and the Chair in particular should keep the discussion away from excessive detail and micromanagement.

It is good practice to divide large strategic decisions into stages, so that the Board can give each stage detailed attention before moving to the next: for instance, discuss the concept of a project first, then challenge the assumptions on which it is based, then analyse the risks and the budget, and only then take the final go-ahead decision.

To get through a long agenda, not all decisions should be treated in the same way: strategic choices should receive enough time for debate, while reports need to be presented only where there are critical matters.

Voting. After the discussion, Board members state whether they are for or against the proposed decision. Decisions are adopted in accordance with the voting rules in the company's internal documents. It is good practice to organise the debate so as to reach unanimous decisions where possible: Boards act effectively when they speak with one voice outside the boardroom.

Assessment of the decision-making process. Once a significant decision has been taken, the Board may find it useful to review the effectiveness of the process immediately after the meeting and, where relevant, the merits of the decision itself. This can also be a topic in the Board evaluation questionnaire.

Traps that lead to poor decisions:

- a dominant personality or group of members on the Board, inhibiting contribution from others;
- insufficient diversity of perspective on the Board, which contributes to groupthink;

- a compliance mindset and failure to treat risk as part of decision-making;
- insufficient knowledge and ability to test underlying assumptions;
- failure to recognise the consequences of running the business on the basis of self-interest and other poor ethical standards;
- a lack of openness by management, a reluctance to involve non-executive members, or a tendency to bring matters to the Board for sign-off rather than debate;
- complacent or intransigent attitudes;
- inability to challenge effectively;
- inadequate information or analysis;
- poor quality papers;
- lack of time for debate, or truncated debate;
- undue focus on short-term horizons;
- insufficient notice.

KEY TAKEAWAYS

A. The quality of a decision depends on the quality of the process: an analysis of the facts, a proper procedure and a record that shows how the decision was reached.

B. Before deciding, each Board member should ask whether the Board is the right body, whether there is a conflict of interest, what problem is being solved, whether the decision is in the company's best interests and in line with strategy, what the alternatives, costs, benefits and risks are, whether the information and assumptions are sound, and how the decision will be communicated and monitored.

C. The Chair guides the discussion, ensures that major proposals are challenged, invites every member's opinion and speaks last; the Board relies on management's materials but may obtain independent expert advice, and must avoid groupthink and micromanagement.

D. Large strategic decisions are best taken in stages, from concept through assumptions, risks and budget to the final go-ahead, and not all agenda items deserve the same time.

E. Decisions are adopted under the voting rules in the company's internal documents, ideally by consensus, and the Board speaks with one voice outside the boardroom; the effectiveness of the process itself should be reviewed after significant decisions.

QUESTIONS FOR THE BOARD

1. *Before our last significant decision, did the Board consider the alternatives, the risks and the assumptions, or only the proposal put to it by management?*
2. *Does the Chair make sure that every member speaks before giving their own view, and are major proposals challenged rather than rubber-stamped?*
3. *When did the Board last obtain independent advice on a complex matter, and how did it decide that it was needed?*
4. *Are large strategic decisions taken in stages, and does the Board give strategic choices more time than routine reports?*
5. *Which of the traps that lead to poor decisions could apply to our Board, and how would we know?*

6.4

BOARD COMMITTEES – WORKING METHODS

The role and composition of the committees are described in sub-chapter 3.4; this sub-chapter deals with their working methods.

Responsibilities and authority of committees

Committees facilitate the Board's work through monitoring, information, advice and the preparation of decisions to be taken by the Board. Committees should exercise independent judgement and integrity in performing their functions and in deciding on their recommendations to the Board. The recommendations are not binding; the final decision is taken by the Board.

Committee members are expected to act in good faith, dedicate the necessary time to the tasks delegated by the Board, exercise due diligence, be thorough in pursuing their duties, alert the Board to developments and risks in their areas and report to the Board in good time to support its decisions. In return, the Board is expected to delegate responsibilities to committees in a reasonable manner and to give them the expertise, resources and information they need.

Reporting to the Board

The committee charter should include reporting rules to ensure accountability to the Board.

Regular committee reports should highlight only the most important issues emerging from the committee's discussions: the things the full Board really needs to know.

If a committee meets just before a Board meeting, the committee chair presents an oral or written summary of the key points, with the minutes or report to follow.

The minutes of the committee, or its report, should be available to the Board. The secretary of the committee is responsible for taking the minutes of each meeting.

The committee submits an annual report to the Board.

Disclosure of Board committees in the annual report

Companies should also include in their annual reports information on the existing Board committees: their composition, the number of meetings and attendance

during the year, and the main areas of their activity and their performance, in compliance with the rules on the processing of personal data.

Technical environment

Providing the right tools is important for effective committee work: tools that allow committees to collaborate, communicate, share and review documents, set agendas, work on preparatory materials, distribute minutes and publish results.

Key elements of effective Board committees

There is no one-size-fits-all approach to Board committees; the key elements that increase their effectiveness are:

- a clearly defined purpose, duties and composition;
- clearly defined rules governing the committee's activities;
- regular and timely meetings;
- established reporting process;
- integration of the committee into the company's processes;
- the right tools for the committee's work.

KEY TAKEAWAYS

A. Committees facilitate the Board's work through monitoring, information, advice and the preparation of decisions; their recommendations are not binding, and the final decision is taken by the Board.

B. Committee members act in good faith, dedicate the necessary time, exercise due diligence and alert the Board to developments and risks in their areas; the Board in turn delegates reasonably and provides the expertise, resources and information required.

C. The committee charter sets the reporting rules; regular reports highlight only what the full Board needs to know, the committee chair summarises key points at the next Board meeting, minutes or reports are available to the Board and an annual report is submitted.

D. The annual report of the company discloses the committees, their composition, the number of meetings, attendance and main areas of activity.

E. Effective committees have a clearly defined purpose, duties and composition, clear rules, regular and timely meetings, an established reporting process, integration into the company's processes and the right tools.

QUESTIONS FOR THE BOARD

1. *Does each committee have a charter with a clear purpose, duties, composition and reporting rules, and when was it last reviewed?*
2. *Do committee reports tell the full Board what it needs to know without repeating the committee's whole discussion?*
3. *Does the Board give its committees the time, expertise, information and tools they need, and does it evaluate their effectiveness?*
4. *Are the committees, their composition, meetings and attendance disclosed in the annual report of the company?*
5. *Is the Board clear that committee recommendations prepare its decisions but do not replace them?*

6.5
BOARD SECRETARY

Who is the Board secretary

The duties of a Board secretary vary from company to company, depending on the type of company, the sector in which it operates and the structures, policies and procedures it adopts.

Whatever the company, the Board secretary usually plays a valuable role as a bridge for information, communication, advice and arbitration between the Board and management, and between the company and its stakeholders, including its shareholders. The Board secretary can help management to understand the requirements of the Board, help the Board to understand the challenges management faces in meeting them, and help the company to manage stakeholder relations. The role therefore involves, in addition to compliance, working with people to create the culture that allows the governance structures, policies and procedures to work effectively.

There are several ways of establishing the Board secretary function, and choosing the right one is an important governance decision. The three main models are described below.

1. **The chief legal officer (CLO) model**
   In this dual role the company's most senior lawyer also serves as secretary to the Board. It is a common choice in medium-sized and large companies seeking streamlined communication with the executive. It brings efficiency and authority: deep knowledge of the company's legal risks and strategy is immediately available to the Board, and the CLO carries the weight needed for governance advice to be taken seriously. The challenges are workload and conflicts of interest: the dual burden can lead to overload or a lack of attention to administrative precision, and the CLO may struggle to remain an objective guardian of governance when their own executive legal decisions are under the Board's scrutiny.

2. **The dedicated in-house secretary**
   A dedicated employee, typically a lawyer or governance professional, is appointed solely to manage the Board's affairs and usually reports directly to the Chair. This model provides focus and independence: undivided attention to Board logistics, minutes and relations with Board members, and a more neutral perspective on procedural compliance than the CLO can offer. Without broader

operational duties, however, the secretary may lack the wider context of the company's day-to-day legal challenges.

3. **The external professional model**
   The company outsources the function to a specialised governance firm or external legal counsel. This gives the company and the Board access to experts who keep abreast of evolving governance rules across several industries. An outsider may, however, lack an intuitive understanding of the company's internal knowledge and interpersonal dynamics, and may not be available for urgent, last-minute consultation while serving other clients.

Appointment and required skills

It is best practice for the Board secretary to be appointed and removed by the Board, which should ensure that the person appointed is capable of carrying out the role.

The skills required of a good Board secretary include:

- respectful, diplomatic and effective communication;
- active listening;
- bringing issues to the surface, especially those relating to reputational risk;
- identifying common concerns and interests;
- generating alternative solutions;
- respecting confidences;
- appreciation of all parties;
- disagreeing constructively;
- a commercially minded approach.

The Board secretary is responsible to the Board and accountable through the Chair for all matters relating to their core duties to the Board.

Role and functions

The role of the Board secretary includes the following key functions:

- ensuring compliance with governance procedures;
- communication with Board members;
- communication between the Board and management;
- shareholder relations and the organisation of shareholder meetings;
- acting as the conscience of the company;
- ensuring compliance with laws and regulations;

- organising induction training for newly elected Board members;
- managing the company's corporate governance framework.

The functions and responsibilities of the Board secretary are set out in Annex 7.

KEY TAKEAWAYS

A. The Board secretary is the bridge between the Board and management and between the company and its stakeholders, helping each side understand the other and creating the conditions for the governance structures and procedures to work.

B. The function may be set up in three ways: the chief legal officer as secretary (authority and efficiency, but workload and conflicts of interest), a dedicated in-house secretary (focus and independence, but less operational context) or an external professional (specialist expertise, but less internal knowledge and availability).

C. The Board secretary is appointed and removed by the Board, is responsible to the Board and accountable through the Chair, and needs diplomacy, active listening, the courage to surface issues, discretion and a commercial mindset.

D. The key functions cover governance procedures, communication with and between the Board and management, shareholder relations and meetings, compliance with laws and regulations, induction of new members and management of the governance framework; a checklist of tasks is provided in Annex 7.

QUESTIONS FOR THE BOARD

1. *Which model of Board secretary do we use, and does it give the Board the independence, expertise and availability it needs?*
2. *Is the Board secretary appointed by the Board and accountable through the Chair, rather than to management?*
3. *Does the Board secretary have the skills, standing and access to bring difficult issues, including reputational risks, to the Board's attention?*
4. *Are the key functions of the Board secretary defined in writing, and are induction of new members and management of the governance framework among them?*
5. *How does the Board assess the quality of the support it receives from the secretary?*

6.6

BOARD PERFORMANCE EVALUATION AND IMPROVEMENT ACTION PLAN

The effectiveness of the Board affects the performance and success of the whole company, so the Board should improve its performance constantly. It should demonstrate performance and leadership in guiding management and provide valuable support to the top executives, which only a professional, effective and engaged Board can do. Board should carry out a self-evaluation and report (preferably in the annual report) a summary of key findings and performance improvement plan to the shareholders.

The self-evaluation should be guided by the Chair of the Board. The Board may, however, decide to engage an external facilitator to assist in preparing the questionnaire and in leading the Board discussions.

While the Board performance evaluation is owned and led by the Chair of the Board, appropriate involvement of top management can provide valuable insight into the effectiveness of the interaction between the Board and management. Such input should be structured, clearly defined in scope and focused on areas where management has direct experience, such as the quality of the strategic dialogue, the clarity of guidance and the effectiveness of decision-making processes. At the same time, safeguards should be in place to preserve the independence of the evaluation, ensuring that management's input complements, but does not influence or constrain, the Board's own assessment and conclusions. The questionnaire for top management will differ from the Board's questionnaire and should have an introductory part explaining the Board's expectations and how to carry out this important exercise (see the example in Annex 9).

A thorough annual self-evaluation is one of the key tools for developing the Board's performance and effectiveness continuously. The Board's work is complex and each Board member is different, so there are many aspects that the Board could and should discuss during the self-evaluation.[29]

The key success factors of a self-evaluation that produces real improvement are:

– Purpose. A genuine desire to build a high-performing Board that is equipped to anticipate, meet and overcome future challenges and to ensure alignment with the company's long-term strategy.

29 G20/OECD Principles of Corporate Governance (2023), Principle VI.E.4, which recommends that Boards regularly carry out evaluations to appraise their performance and assess whether they possess the right mix of background and competences.

- Scope. The evaluation should cover the Board as a collective body, the Board members individually and the Chair.
- Preparation. The most important step is to create, or revise, the self-evaluation questionnaire (see Annex 8 for an example).
- A clear plan. The Chair, with the help of the Board secretary, develops and communicates the plan for the whole process and allocates the resources needed to support it.
- Open and objective discussion. Each member and the Board as a whole must be fully open and objective in discussing their own performance and that of the Board; only then can the areas for improvement be identified.

The self-evaluation process can be divided into the following stages:

1. **Planning.** Create and agree a self-evaluation plan, including the meeting schedule, specific tasks and the people involved.
2. **Questionnaire.** Develop a questionnaire covering the Board's work and engagement. It is good practice to review the existing questionnaire with the whole Board before each annual self-evaluation and to make the necessary amendments. It is important not only to give a score but also to provide comments where the score is not the highest. A separate questionnaire should be developed for top management (see the example in Annex 9).
3. **Evaluation.** Each Board member completes the questionnaire, and all evaluations and comments are consolidated. Each manager completes the management questionnaire.
4. **Results and action plan.** Board members discuss the consolidated results of both questionnaires and provide comments. After the discussion, the Board agrees on the common evaluation results and develops an improvement action plan (topic, deadline, responsible person; see Annex 10). The Board work improvement action plan may be presented to the shareholders to show them how the Board is seeking to improve its performance.
5. **Follow-up.** The Board supervises the implementation of the plan and reviews it at least twice a year (in the middle of the year and after the year-end).

It is good practice to carry out an **external evaluation** every three years, with the help of experienced consultants. Its benefits are:

- transparency, independence and greater objectivity;
- possible benchmarking against other Boards;
- a more thorough and impartial identification of strengths, skills and weaknesses, examined against the company's business goals and changing environment;

– a broader range of views and ideas on how to improve Board effectiveness including possible changes to the Board's composition.

Ultimate responsibility for the evaluation, internal or external, lies with the Chair of the Board.

The same principles are applicable to the committees' performance evaluation as they are set to the Board's evaluation.

It is recommended that the Board reports on the evaluation process to the general meeting of shareholders, describing the main outcomes, the actions taken or planned and how these affect the Board's future composition and effectiveness. The report should give a concise and clear summary of the process and its results, without disclosing information that is commercially confidential or could harm the company's interests. Such reporting allows shareholders to assess the Board's competence and, if necessary, hold it accountable at the annual general meeting, and helps to ensure that the Board operates in a way that promotes the company's long-term success. Further guidance on Board evaluation is provided in the ecoDa Board Evaluation Recommendations.[30]

KEY TAKEAWAYS

A. A professional, effective and engaged Board improves its performance constantly; an annual self-evaluation of the Board, its members, the Chair and the committees is the key tool for doing so.

B. The self-evaluation is led by the Chair with the support of the Board secretary, and its success depends on a genuine purpose, a clear scope, a well-prepared questionnaire, a clear plan and open and objective Board discussion.

C. Structured input from top management on the quality of Board–management interaction adds insight, provided that the evaluation remains independent and management's input complements rather than constrains the Board's own conclusions.

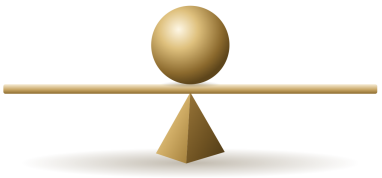
D. The process runs from planning and questionnaire through evaluation to an agreed improvement action plan with topics, deadlines and responsible persons, followed up at least twice a year.

E. An external evaluation every three years brings independence, objectivity and benchmarking; the Board reports on the process and its outcomes to the general meeting without disclosing confidential information.

30 ecoDa (2025), Board Evaluation Recommendations, available at https://www.bicg.eu/wp-content/uploads/2025/07/20250617-ecoDa-Board-Evaluation-Recommendations.pdf.

QUESTIONS FOR THE BOARD

1. *When did the Board last evaluate itself, its Chair, its members and its committees, and did the evaluation lead to an action plan with owners and deadlines?*
2. *Was the questionnaire reviewed and updated before the last evaluation, and did members add comments rather than scores alone?*
3. *Did top management contribute structured input, and were safeguards in place to keep the evaluation independent?*
4. *Has the improvement action plan been followed up during the year, and what has actually changed?*
5. *When was the last external evaluation, and did the Board report on the evaluation process and its outcomes to the shareholders?*



CHAPTER

7

CORPORATE GOVERNANCE OF COMPANY GROUPS

How a parent company governs its subsidiaries: governance models, group policies, intra-group transactions and the position of minority shareholders.

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7.1
INTRODUCTION TO GROUP GOVERNANCE

A common structure of a company group is a holding company that owns several subsidiaries (controlled entities), often with different business lines. In a group, decision-making is more complex than in a stand-alone company, so it is important to establish a group governance framework. The Board of the holding company should assume responsibility for governance across the group. It exercises this responsibility by adopting a framework that sets out how the relationship between the holding company and its subsidiaries is structured and managed.

7.2

ADDRESSING THE GROUP GOVERNANCE CHALLENGES

Every company, whether a holding company or a subsidiary, is a separate legal entity with its own rights and obligations. The objective of the holding company is to achieve the group's strategic targets while respecting the roles and boundaries of the subsidiary and its Board members.

A common perception is that Board members nominated to subsidiary Boards by the holding company (the controlling shareholder) act as "representatives" of that shareholder. In principle, nominee Board members owe their duties to the company on whose Board they serve and are required to act in the best interests of all its shareholders, not solely for the benefit of the shareholder that nominated them. Shareholders should therefore always be mindful of the fiduciary duties that apply to Board members. Shareholders usually form subsidiary Boards with a majority of related Board members, to ensure that the necessary decisions are adopted, while an external perspective is obtained through the participation of non-executive or independent Board members.

The holding company usually achieves its group governance targets through the following main measures:

- establishing the group corporate governance framework (purpose, mission, vision, values, strategy, objectives and policies);
- ensuring clear communication of the group's general strategy and objectives;
- appointing the holding company's representatives to subsidiaries' Boards;
- setting the consent rights of the shareholders' meeting (the holding company) for specific matters;
- approving corporate policies and procedures for key matters, to be adopted by the subsidiaries;
- participating in the selection of the CEO at subsidiary level;
- ensuring regular monitoring meetings between representatives of the holding company and of the subsidiary;
- establishing a unified and efficient internal audit function within the group;
- participating in the selection of the external auditor of subsidiaries;
- implementing unified and efficient risk management practices;
- setting and monitoring key strategic indicators;
- centralising competencies and functions within the holding company.

Being required to act in the best interests of the subsidiary does not mean that the members of the Board of a subsidiary should disregard the role, expectations or strategic direction of the holding company. Effective cooperation with the holding company, including alignment with the group's overall objectives, may also be in the best interests of the subsidiary, provided that such alignment is consistent with the subsidiary's own legal duties, business needs, risk profile and stakeholder interests.

At the same time, the subsidiary Board should not treat group interests as automatically overriding the interests of the subsidiary. The subsidiary is a separate legal entity, and its Board has a duty to act in the interests of that subsidiary. This means that the Board should assess group strategies, policies, targets, transactions and decisions from the perspective of the subsidiary and should satisfy itself that they are appropriate for the subsidiary before approving or implementing them.

The relationship between the subsidiary and the holding company should therefore be based on cooperation, transparency and proper governance, rather than automatic subordination. The subsidiary Board should have an effective opportunity to provide input on matters affecting the subsidiary, including at holding company level where relevant. This is particularly important where group policies, internal processes, financing arrangements, shared services, intra-group transactions, risk management frameworks or strategic initiatives may have a material impact on the subsidiary.

The subsidiary Board is primarily responsible for overseeing the management, performance, risk profile and operations of the subsidiary. It should also contribute to the effective integration of the subsidiary within the wider group where this supports the subsidiary's interests. However, decisions should not be justified solely on the basis that they benefit the group or the holding company. Where a proposed decision benefits the group but may create disadvantages, risks or obligations for the subsidiary, the subsidiary Board should carefully assess the implications, consider whether appropriate safeguards or compensating measures are needed, and ensure that the decision can be properly justified as being in the interests of the subsidiary.

In practice, good group governance requires a balanced approach: the subsidiary should be aligned with the group where this is appropriate, but the subsidiary Board must retain sufficient independence, information and authority to discharge its own duties. Group coordination is important, but it should not remove the responsibility of the subsidiary Board to exercise judgement in the interests of the subsidiary.

7.3

MAIN GROUP GOVERNANCE MODELS

Holding companies may choose different parenting strategies, ranging from a hands-off strategy, with no ambition to exercise central control over strategic or operating functions and with the business units managed as purely financial assets, to a hands-on strategy, in which the holding company becomes deeply involved in the management of the business units by influencing operating decisions at the level of the individual business. Different models may be applied to different subsidiaries, depending on the goals set. The four main models are compared in the table below.

Table 7.1 **Main group governance models** [31]

	INVESTMENT MANAGEMENT	STRATEGIC MANAGEMENT	ACTIVE MANAGEMENT	OPERATIONALLY INVOLVED MANAGEMENT
Description in simple words	"We just want to know your results"	"We want to know what you do"	"We want to know how you do it"	"We will work with you to do it"
Who we are	A holding company or head office	The strategic leadership of a collection of subsidiaries	Both consultants to, and the strategic leadership of, the subsidiaries	The key managers of all subsidiaries
Who creates value	Head office creates and enforces a disciplined management model; value is created by the individual subsidiaries closest to customers	Head office adds value in the linkages between subsidiaries; value is created by the individual subsidiaries closest to customers	Head office provides guidance to subsidiaries through its expertise; value is created by the subsidiaries using head office expertise	Head office makes the key decisions for subsidiaries; value is created by head office expertise and control

31 Adapted from Couto, V., Neilson, G. and Karlsson, P.-O. (2008), A Lean, Global Corporate Core: Putting Headquarters in Its Place, Booz & Company (now Strategy&, PwC).

	INVESTMENT MANAGEMENT	STRATEGIC MANAGEMENT	ACTIVE MANAGEMENT	OPERATIONALLY INVOLVED MANAGEMENT
Responsibility	Head office sets high financial goals; subsidiaries are fully accountable for achieving results. Subsidiaries commit to multi-year strategic plans; if these are met, no annual review is necessary	Head office sets key financial and operational metrics; subsidiaries are accountable for results. Subsidiaries commit to multi-year plans; head office ensures strategic coherence across subsidiaries and performs an annual review	Head office and subsidiaries share responsibility for a broad set of financial and operating metrics. Head office proactively reviews subsidiaries' strategic plans and annual budgets	Head office is responsible for financial and operating performance. Head office dictates subsidiaries' strategic plans and budgets
Centralisation of functions	Decentralised: core and support functions are separate in each subsidiary	Partially centralised: core and support functions are separate in each subsidiary, but central support functions at head office govern the overall synergy between subsidiaries	Centralised at head office: core functions remain in each subsidiary; support functions are at head office only	Centralised at head office: core and support functions are at head office only; the subsidiaries execute plans and daily tasks
Mechanisms of integration	None	Moderate	Extensive	Extensive
Appraisal of subsidiary performance	Based on achieving financial objectives	Based on achieving financial and strategic objectives	Based on achieving plans	Based on achieving tasks
Subsidiary incentives and remuneration	Based on the subsidiary's performance	Based on the subsidiary's performance, but also linked to head office	Based on overall group performance	Based on overall group performance

7.4
GROUP POLICIES

What policies are

Policies are usually high-level statements of the main principles according to which decisions are taken and activities are carried out within an organisation. In a group context, policies should clearly explain how the group is governed and how key functions are performed. At the same time, policies should not be overly detailed, as operational details are normally set out in other internal documents, such as procedures, manuals, instructions or guidelines.

Why policies matter

Group policies help to ensure consistency, transparency and discipline across the group. They also support a common governance framework, shared standards of conduct and more predictable decision-making. Well-designed group and company policies:

- drive strategic planning and help to set expectations and performance objectives;
- provide an understanding of the goals and culture of the company;
- engage and align the values of stakeholders;
- lead to more efficient internal operations, as there is no need to discuss how to handle an issue each time it arises, and streamline the induction of new staff;
- ensure accountability;
- create transparency;
- promote ethical and responsible decision-making;
- assess and mitigate risk.

What group policies cover

Group policies may include codes of conduct and ethics, as well as policies applicable to specific types of decisions, functions or areas of activity. Common examples are policies on the approvals framework and delegation of authority, contracts and commitments, investments, financial accounting, risk management, internal control, compliance, conflicts of interest, related party transactions, information management, human resources, sustainable development and, for listed entities, market disclosure and communications. Policies also commonly address culture, values and relationships between people within the organisation. An indicative list of policy topics is given in Annex 2.

Adopting group policies at subsidiary level

In a group of companies, holding companies often develop group-wide policies with the intention that they should apply across the whole group. However, the Board of each subsidiary should not adopt such policies automatically. Each subsidiary is a separate legal entity, and its Board must act in the best interests of that subsidiary, taking into account its own legal duties, business model, risk profile, regulatory environment, financial position, minority shareholders, creditors, employees and other relevant stakeholders.

Therefore, the Board of a subsidiary should review each group policy carefully before approving or implementing it at subsidiary level. The Board should consider whether the policy is appropriate for the subsidiary, whether it complies with applicable local law and regulation, whether it reflects the subsidiary's specific circumstances, and whether any amendments, exceptions or additional procedures are required. Where necessary, a group policy should be adapted to the needs of the subsidiary rather than adopted in identical form.

This does not mean that subsidiaries should ignore or unnecessarily depart from group standards: a coherent group policy framework is important for effective governance, risk management, compliance, internal control and reputation management. Group consistency should, however, be balanced with the subsidiary Board's independent responsibility to ensure that each policy is suitable for the subsidiary and supports its own interests and long-term sustainable success.

7.5

INTRA-GROUP TRANSACTIONS, FINANCING, MINORITY SHAREHOLDERS AND INFORMATION FLOWS

Companies in a group deal with each other constantly: they buy and sell goods and services, share support functions such as IT, finance, human resources or procurement, license brands and know-how, and provide guarantees. Each of these is a ***related party transaction*** (see sub-chapter 5.3.5). The subsidiary Board should satisfy itself that intra-group transactions are concluded on arm's length terms, that the allocation of shared-service costs is transparent and reflects the services actually received, and that the subsidiary is not made to bear costs or risks for the benefit of other group companies. Material intra-group transactions should be approved by the subsidiary Board, documented in written agreements and disclosed in accordance with the applicable accounting and, for listed companies, market rules. Transfer pricing rules add a tax dimension that neither Board should overlook.

Group financing arrangements, such as cash pooling, intra-group loans and guarantees and dividend policies set at group level, deserve particular attention. They are efficient for the group, but they can move liquidity and risk from one entity to another. The subsidiary Board should ensure that the subsidiary retains enough liquidity to meet its own obligations; that loans and guarantees provided to the holding company or to other group companies are on market terms, secured where appropriate and within the limits set by company law on capital maintenance and distributions; and that the subsidiary would not be put at risk if the holding company or another group company ran into financial difficulty.

Where a subsidiary has ***minority shareholders, the balance of interests*** becomes more delicate. Minority shareholders bear part of the subsidiary's risk but have no say in group decisions, so they are exposed to the holding company using its control to extract value, for instance through transactions on unfavourable terms, excessive management fees or the diversion of business opportunities to other group companies. The subsidiary Board should treat all shareholders equitably; Board members with a conflict of interest should abstain from decisions on transactions with the holding company; and independent Board members, the audit committee or an independent fairness opinion should be involved in material related party transactions. The company laws of the Baltic states give minority shareholders rights of information and of challenge, and listed companies are subject to the related party transaction rules described in sub-chapter 5.3.5.

Finally, the Board of the holding company can discharge its responsibility for governance across the group only if it ***receives adequate information from the subsidiaries***. The group governance framework should define what the subsidiaries report and how often: at a minimum, financial results against budget, key performance and risk indicators, compliance and whistleblowing matters, material litigation, major transactions and events, and the results of internal and external audits. Reporting should follow a consistent format across the group, subsidiary Boards should know what is reported upwards, and the holding company Board should in turn ensure that its own decisions and expectations reach the subsidiaries clearly and in good time. Regular meetings between the holding company's representatives and the subsidiary's Board and management complement the written reporting. In regulated sectors and in listed groups, the exchange of information within the group must also respect the rules on confidential and inside information and on data protection.

KEY TAKEAWAYS

A. A company group is a set of separate legal entities. The Board of the holding company is responsible for governance across the group and sets the framework that defines how the relationship with the subsidiaries is structured and managed.

B. Board members nominated by the holding company owe their duties to the subsidiary on whose Board they serve. Alignment with the group is usually in the subsidiary's interest, but the subsidiary Board must assess every group policy, transaction and decision from the subsidiary's own perspective.

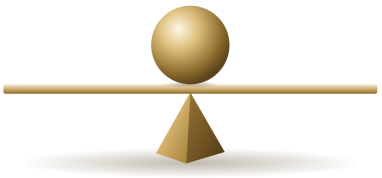
C. The holding company can choose between four parenting models, from investment management to operationally involved management, and may apply different models to different subsidiaries. The choice determines how functions are centralised, how performance is appraised and how incentives are set.

D. Group policies bring consistency and discipline, but each subsidiary Board should review them, check their compliance with local law and adapt them where necessary before adopting them.

E. Intra-group transactions, shared services and group financing must be on fair terms, approved and documented; the subsidiary Board protects the subsidiary's liquidity and the equitable treatment of its minority shareholders, and the group governance framework defines what information the subsidiaries report to the holding company Board and how often.

QUESTIONS FOR THE BOARD

1. *Do we have a written group governance framework that sets out the roles of the holding company and the subsidiaries, the matters requiring the holding company's consent and the reporting lines?*
2. *Which parenting model do we apply to each subsidiary, and is it the right one for that subsidiary's business, risks and maturity?*
3. *Do the members we nominate to subsidiary Boards understand that their duty is to the subsidiary, and how do we handle situations where group and subsidiary interests differ?*
4. *Have all group policies been reviewed and formally adopted by each subsidiary Board, with any local adaptations recorded?*
5. *How do we ensure that intra-group transactions, financing and shared services are on fair terms and do not disadvantage a subsidiary or its minority shareholders?*
6. *Are internal audit and risk management organised group-wide, and does the Board of the holding company receive sufficient and timely information on the subsidiaries?*



CHAPTER

8

LIABILITY OF BOARD MEMBERS AND MITIGATION TOOLS

When Board members can be held personally liable, and which tools – including D&O insurance – help to manage that risk.

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8.1
LEGAL LIABILITY OF BOARD MEMBERS

Although all corporate and business decisions at Board level are adopted collectively, each individual Board member can, in certain circumstances, be held personally liable for the improper performance of their duties as a Board member. Depending on the type of unlawful conduct, a Board member may be subject to civil, administrative or criminal liability. Main principles of the statutory and case law on the Board liability are briefly described below to give Board members a better understanding of how liability works and guidance on how to identify and mitigate the associated risks.

Civil liability

This is the most common type of liability that may arise for a Board member for breach of their duties. The general principle is that a Board member may be held personally liable if they fail to perform their duties as a Board member and the company or a third person has incurred damage as a result.

The conditions for civil liability to arise are:

1. unlawful actions of the Board member (breach of statutory duties, fiduciary duties or the general duty of care);
2. damage incurred by the company or another person as a result of such unlawful actions;
3. a causal link between the unlawful actions and the damage; and
4. the fault of the Board member (which is presumed if the claimant proves the unlawful actions).

Under the law, the Board member is presumed to have acted lawfully and in the best interests of the company until it is proved otherwise, which means that the burden of proving that all the above conditions (except fault) are met lies with the person claiming damages.

In the vast majority of cases the claimant is the company on whose Board the defendant serves. Either the company itself brings a claim against the Board member, or a shareholder does so on behalf of the company by way of a derivative claim. If a derivative claim is successful, damages are awarded to the company and not to the shareholders who claimed on its behalf. Creditors also have the legal right to bring direct claims against Board members. In such cases, however, it has to be proved that the unlawful actions of the Board member were directed specifically against the claiming creditor, who as a result incurred individual

damage, that is, damage not incurred by the company or its other creditors (for example, where a Board member knowingly submitted incorrect information to a creditor, who was thereby misled into entering into a detrimental contract with the company). Creditors usually claim personal liability from Board members where the company is already insolvent and unable to satisfy creditors' claims in full.

The civil liability of Board members is personal, not collective. Board members do not automatically become personally liable if the Board as a whole does something that results in damage to the company: all the conditions for civil liability (except fault) have to be proved in respect of each Board member individually. For this reason, a Board member who voted against a Board decision that later turned out badly may be exempted from personal liability, whereas those who voted in favour could be held personally liable (provided, of course, that all the other conditions are met). As between the Board members, civil liability is joint and several, which means that the claimant may claim the entire damage from one or several Board members, who may later recover the respective shares from the remaining Board members.

It is very important to note that the approval of the shareholders or of the Board does not in itself relieve Board members from personal liability for breach of their duties. Each Board member must therefore at all times exercise independent judgement when performing their duties and avoid relying solely on the decisions of other corporate bodies of the company.

Business judgement rule and similar mechanisms to address risk aversion

The business judgement rule (BJR) is a central doctrine of corporate law that protects Board members from liability when business decisions turn out poorly, as long as those decisions were made properly.

Under the rule, courts will not review the business decisions of the Board if they were made:

1. in good faith, with honest intentions and no conflicts of interest;
2. with due care, on the basis of sufficient information and deliberation;
3. within the Board's authority, that is, within its powers under the law and the company's documents;
4. in the best interests of the company, even if the outcome was negative.

The aims of the BJR are:

– to encourage reasonable risk-taking, as business involves uncertainty and leaders need the freedom to innovate without fear of lawsuits for every failure; (

- to prevent hindsight bias, so that courts do not judge decisions only by their outcomes, since even careful choices can lead to losses; and
- to balance accountability and autonomy, which means that although Board members must be loyal and careful, they should not be punished for every misstep if they acted responsibly.

The business judgement rule was developed by the US courts to strike the right balance between the positive aspects of risky business decisions and the limitation of the Board's liability for business decisions that turned out to be unsuccessful. The rule was later adopted in many European jurisdictions, including Lithuania; certain aspects of it, but not the rule itself, are also applied in Latvia and Estonia too.

Lithuania

Lithuanian case law recognises that doing business inherently involves taking risks and that it would be unreasonable to hold Board members liable for business decisions that were adopted in good faith but later turned out to be detrimental to the company. The general principle is that a Board member may not be held personally liable for a business decision unless it is proved that, in arriving at that decision, they manifestly exceeded the reasonable limits of business risk or otherwise clearly acted in a grossly negligent manner. In cases where personal liability is claimed for a business decision, a higher burden of proof therefore applies, which protects Board members and allows them to take business risks on behalf of the company. Board members lose this protection, however, if the claimant shows that they acted in breach of their duty of loyalty, their duty of care or mandatory provisions of the applicable law (for example, provisions on the competence of the Board).[32]

Thus, the two key rules that Board members must follow in order to remain protected by the business judgement rule are:

1. Board members must always disclose all actual and potential conflicts of interest related to a particular business decision and recuse from participating in taking or in any way affecting tje business decisions in relation to which they have or may have a conflicting interest; and
2. Board members must exercise due care in adopting business decisions, which involves analysing and considering all the available information on the decision, collecting any additional information necessary to arrive at an informed decision (for example, by obtaining expert opinions), analyse all pertinent risks and

32 Civil Code of the Republic of Lithuania, Article 2.87 (duties of members of the bodies of a legal person); the business judgement rule has been developed in the case law of the Supreme Court of Lithuania.

consider how they will be managed, performing cost-benefit analysis of the proposed decision.

Latvia

There is no business judgement rule in Latvia, so, to avoid liability for the damages claimed, the Board member has to prove that they:[33]

1. acted as a prudent and careful manager. The principle of the "prudent and careful manager" is an objective standard, that is, what could be expected from a prudent and careful manager in business generally and in the specific line of business (a higher standard applies, for example, to entities in highly regulated sectors such as financial institutions); and
2. acted in good faith within the framework of a lawful decision of the shareholders' meeting.

Estonia

In Estonia, Board members are liable for any type of negligence, and there is no clear expression of the business judgement rule. The courts, however, distinguish between the decision-making process and the outcome of the Board member's act and have held that Board members are not liable solely because their business decisions were detrimental to the company.

Under Estonian corporate law, the obligations of Board members must be performed according to certain standards, primarily:

1. the standard of care;
2. the duty of loyalty.[34]

The standard of care includes the obligation of a Board member to act, in their decision-making, in the most economically purposeful manner. This standard is normally considered met if the Board member (i) is diligent, (ii) is sufficiently informed to take the decision and (iii) does not take unreasonable risks for the company. A Board member is normally considered sufficiently diligent if (i) they have no personal conflicting interest, (ii) they are informed to a degree that can be considered reasonable in the circumstances and (iii) a *bona fide* Board member in a similar situation could reasonably believe that the action or decision is in the best interests of the company.

33 Commercial Law of the Republic of Latvia, Section 169 (liability of Board members; the standard of the honest and careful manager).
34 Commercial Code of the Republic of Estonia, § 187 and § 315 (liability of members of the management board of a private limited company and of a public limited company).

The duty of loyalty requires the Board member to act in the interests of the company (and not, for example, in the interests of only one or some of the shareholders) and to ensure that their decisions are not affected by their personal interests.

Release of Board members from liability by the company

The laws of each of the three Baltic states allow the company (the shareholders' meeting) to release the Board or its members from liability. Although the laws vary in their details (for example, a general release or a release for specific actions or losses that have already occurred) and in the procedure, in all cases such a release:

1. is not valid in respect of conduct that was wilful or grossly negligent on the part of the Board or the Board member; and
2. does not prevent claims by shareholders who voted against the release, by creditors, by the bankruptcy administrator of the company or by other third parties with a right of claim against the Board or its members.

Administrative and criminal liability

Unlike managers of companies, Board members are rarely subject to administrative fines for breach of their duties. Board members may, for example, be found liable if the Board fails to convene the general meeting of shareholders in time, fails to observe the procedure for convening it, prevents shareholders from participating in it or violates other rights of shareholders.

Examples of crimes for which Board members may be held criminally liable include the misappropriation of company assets, fraud, money laundering, falsification of documents, bribery and tax evasion. Lithuanian law does not contain any special rules on the criminal liability of Board members, which means that it has to be proved beyond reasonable doubt that the Board member participated in the criminal activity.

Risk mitigation tools

Some of the tools commonly used by Board members to manage the risk of personal liability are:

1. understanding the duties and responsibilities of the Board and its members and performing them in a due and timely manner;
2. not intervening in the competence of other corporate bodies (for example, not micromanaging or doing management's work), since such actions may result in the Board or the Board member being held liable as de facto management;

3. clearly voting “in favour” or “against” each decision; there is no option to abstain, as decision-making, not decision avoidance, is one of the main tools, obligations and outputs of the Board;
4. acting at all times in the interests of the company and all its shareholders (not of one specific shareholder or group of shareholders, such as those who nominated the member for election), treating all shareholders and other stakeholders equitably and, whenever the company’s financial situation worsens, taking due account of the rights and interests of creditors, whose interests may take priority over those of the shareholders in a dire financial situation;
5. obtaining D&O insurance (see sub-chapter 8.2);
6. obtaining fairness or expert opinions where important business decisions are adopted;
7. relying on competitive sale processes (for example, selling assets by auction) where possible;
8. creating Board committees with specific functions (for example, a remuneration committee or a nomination committee) to analyse matters more thoroughly and make recommendations to the Board; Board members must not, however, rely blindly on the committee’s work and recommendations and must in each case make their own critical and informed assessment, as the final decision on each matter, and the liability for it, rests with the Board and not with the committee;
9. reviewing business processes and implementing appropriate compliance tools and policies;
10. improving effectiveness of oversight over management;
11. duly documenting the Board’s deliberations, so that the minutes reflect not only the decision taken but also the arguments and grounds on which the Board arrived at it, the risks identified and considered and how they were managed as well as dissenting opinions of members, if any.

A toolbox for staying on the safe side

1. Do not agree to serve on a Board if you are not actually and actively involved in the company’s governance.
2. Do not agree to serve on a Board if there is no trust.
3. Be aware of what is going on in the company, even outside your direct responsibilities.
4. Establish clear reporting systems to keep yourself informed.
5. Establish clear internal communication rules within the Board, between the Board and the shareholders, and between the Board and other key managers.

6. Make and keep your own notes on meetings and decisions, especially on sensitive or important matters, since after the end of your term you must return all information related to the company and your Board work and may not retain it.

KEY TAKEAWAYS

A. Board decisions are collective, but liability is personal: each Board member may be held civilly, administratively or criminally liable for the improper performance of their own duties, and the approval of the shareholders or the Supervisory Board does not relieve them of it.

B. Civil liability requires unlawful action, damage, a causal link and fault; fault is presumed once the unlawful action is proved. Claims are usually brought by the company or by shareholders on its behalf; creditors may claim directly where the company is insolvent and the harm was specific to them.

C. The business judgement rule protects decisions taken in good faith, with due care, within the Board's authority and in the company's interests. Lithuania applies it in case law; Latvia applies the standard of the prudent and careful manager; Estonia distinguishes the decision-making process from the outcome. In all three countries, proper management of conflicts of interest and an informed, documented decision are the minimum conditions for protection.

D. The main mitigation tools are knowing and performing one's duties, staying within the Board's competence, voting clearly, acting for the company and all its shareholders, taking creditors' interests into account when the finances deteriorate, obtaining expert opinions, using committees without relying on them blindly, and documenting the Board's deliberations in the minutes.

QUESTIONS FOR THE BOARD

1. *Do all Board members understand the conditions under which they can be held personally liable in the jurisdiction of the company, and when were they last briefed on this?*
2. *Are conflicts of interest declared and recorded at every meeting, and do conflicted members recused from participating in taking the decision and do not try to affect it in any other way?*
3. *Do our minutes show the information considered, the alternatives, the risks and the reasons for each significant decision, so that the business judgement rule would protect us?*
4. *Does the Board stay within its competence and avoid acting as de facto management?*
5. *Do we obtain independent expert or fairness opinions for major transactions, and do we record how committee recommendations were assessed?*
6. *Has the company's financial position deteriorated to the point where the interests of creditors must be given priority?*

8.2

DIRECTORS' AND OFFICERS' LIABILITY INSURANCE

Directors' and officers' liability insurance (D&O insurance) is a special insurance cover that protects Board members and managers (officers) from personal losses if they are sued by shareholders or any third party.

The main benefits of D&O insurance for Board members, managers, the company and the shareholders are:

- greater ability to attract the best professionals to the Board and to executive positions, because candidates know that they will be protected in a fast-changing business environment full of uncertainties;
- protection of the personal assets of Board members and managers where claims are brought against them personally; the policy may cover defence and litigation costs, helping them to obtain legal representation, participate effectively in dispute resolution proceedings and present their position without bearing these costs personally;
- coverage of the legal defence costs incurred in defending lawsuits or investigations;
- protection of the financial stability of the company by covering legal costs and potential settlements;
- greater comfort for shareholders investing in the company, knowing that a process is in place to resolve possible leadership liability risks.

It is good practice for the company to have a D&O insurance policy. Board members and managers are advised to check the facts about the policy and to ask for its main terms and conditions to be presented to them. When the insurance is renewed, the terms and conditions should be presented to the Board and the managers.

Why do Board members need D&O insurance?

Companies are legal entities separate from the people who manage them. Even in companies which shareholders have limited liability, the liability of Board members is unlimited in many countries. Although most contracts between Board members and the company state that the company will indemnify them, this is not always possible, especially where the law or insolvency prevents it.

Any claim against a Board member, or investigation into their activities, will incur costs in preparation and defence even if the matter does not go to court, and if it does, those costs escalate quickly. The Board member's personal assets will be at risk if they do not have sufficient funds to pay for proper legal and other representation.

Why do companies purchase D&O policies?

In today's ever more complex world, all companies require good management in order to succeed. Good managers understand that they have to make difficult and complex decisions for which they are personally liable. Over and above the indemnification clauses in contracts, companies need to be able to offer secure D&O insurance to attract and retain the best managers.

Who can be covered?

All current, future and past directors and officers of a company and its subsidiaries are covered under a D&O policy, including Board. Employees with a managerial role are often also covered for their exposure to liability in that role, and there are a number of other possibilities to extend cover to additional people and positions.

What can be covered?

The main function of a D&O policy is to protect the personal assets of Board members. In practice, this often means that the policy pays the legal fees of Board members when they defend themselves against a claim or prepare to attend an investigation. If a settlement is to be paid to a third party, the policy will often pay some or all of that cost as well.

Most claims are settled out of court, but court costs are also covered where needed.

What cannot be covered?

D&O policies are "all risks" policies, covering all causes of claims unless excluded, so the policy exclusions are very important. They always include proven illegal acts and claim already made against Board members before the policy incepts. Other common exclusions are pollution claims, claims in the USA and claims for injury and damage to property.

It is important to distinguish between "absolute" exclusions, which remove cover for anything related to the excluded acts, and "for" exclusions, which exclude only claims that are specifically for the alleged act; the latter are preferable. Many exclusions relate to exposures that should be covered under other insurance

policies, such as property or professional liability insurance, so the exclusions should always be checked against the other policies.

The size of the insurance cover

Determining the right size of the D&O cover is very important for each company at each annual renewal. It should involve a careful assessment of the company's risk profile (the higher the risks the company takes, the higher the cover should be), its industry and regulatory environment (a more regulated environment may carry higher risks) and its operational complexity. There is no one-size-fits-all answer, and the recommended amount of cover can vary significantly depending on these factors.

Policy triggers

D&O policies have three main definitions that act as the policy triggers:

1. there needs to be a wrongful act (which generally means anything done or not done by a Board member);
2. there needs to be a claim against the Board member based on that wrongful act; and
3. there needs to be a financial loss for which the Board member is liable as a result of the claim (most often legal costs).

How does D&O insurance work in practice?

1. A Board member (or the whole Board) fails to perform their duties.
2. Someone (the shareholders, the company or another interested person or entity) suffers a loss and decides to claim compensation from the Board.
3. The Board is informed of the claim.
4. The Board engages legal defence.
5. The Board contacts the insurance company or broker and provides the details of the claim.
6. If the claim meets the conditions of the insurance cover, the insurer covers the defence costs.
7. If the claim is covered and the court case is lost, the insurer covers the defence costs and the losses, up to the insured sum.

An experienced and specialised insurance broker is an invaluable partner in this process, with access to claims data, benchmarking studies and in-depth knowledge of the D&O insurance market. In the event of an insured event, the broker should be approached immediately for professional help.

KEY TAKEAWAYS

A. D&O insurance protects the personal assets of Board members and managers against claims by shareholders or third parties, covers defence costs and settlements, supports the company's financial stability and helps to attract and retain good Board members and managers.

B. Cover extends to current, past and future directors and officers of the company and its subsidiaries, including non-executive and Supervisory Board members, and often to employees with managerial roles.

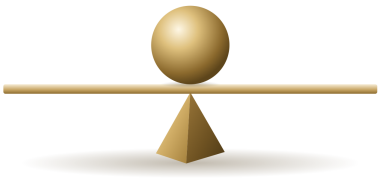
C. Policies are "all risks", so the exclusions matter most: proven illegal acts, claims made before inception, pollution, claims in the USA and injury or property damage are typically excluded; "for" wording is preferable to absolute exclusions, and exclusions should be checked against the company's other policies.

D. The size of the cover is reviewed at each annual renewal against the company's risk profile, regulatory environment and complexity; the policy is triggered by a wrongful act, a claim and a loss; an experienced broker should be involved at renewal and immediately when a claim arises.

E. Board members should ask to see the main terms and conditions of the policy and be informed of any changes at renewal.

QUESTIONS FOR THE BOARD

1. *Does the company have a D&O policy, and have Board members seen its main terms, exclusions and limit?*
2. *When was the size of the cover last reviewed against the company's risk profile, and who made that assessment?*
3. *Are all Board members, Supervisory Board members and relevant managers, including past and future ones, covered, and are subsidiaries included?*
4. *Do Board members know how to notify a claim or an investigation, and is a specialised broker engaged?*
5. *Are the exclusions consistent with the company's other insurance policies, so that no gaps remain?*



CHAPTER

9

FINAL REMARKS: FROM GOVERNANCE RULES TO GOOD GOVERNANCE PRACTICE

Why good governance is ultimately a matter of practice rather than rules, and how to make this Handbook part of the Board's everyday work.

Good corporate governance is a continuous journey towards the long-lasting success of a company. It is not a formal structure, a set of documents or a compliance exercise but **a way in which power, responsibility and accountability are organised within the company**. Its value becomes visible when important decisions are made: when strategy is challenged, risks managed, management held accountable, shareholders treated fairly, conflicts of interest handled appropriately, and the company's long-term interests protected as well as possible.

For Baltic businesses, corporate governance should be understood as **a practical tool for building stronger, more resilient and more trusted companies**. While there are different types of companies - listed, private, family businesses, state-owned and municipal enterprises, start-ups, financial institutions and company groups – and while their governance models will not and should not be identical, the core principles remain the same for everyone: clear separation of roles, competent and independent oversight, integrity, transparency, accountability and a focus on sustainable long-term value creation.

A decisive role in this process belongs to the Boards. A good Board does not manage the company on a daily basis, but it ensures that the company is properly directed and controlled. It sets the tone from the top, challenges and approves strategy, oversees performance, appoints and evaluates management, protects the integrity of reporting and controls, ensuring that both significant risks and opportunities are properly addressed. The effectiveness of governance therefore depends not only on the existence of a Board, but on the quality of its work: preparation, judgement, constructive challenge, independence of mind, ethical conduct and the ability to act in the best interests of the company.

The next stage of governance development in the Baltic region should **move beyond formal compliance**. Many companies already have the basic governance structures. The real question is whether these structures work in practice. Are Board agendas focused on the most important issues? Are Board materials concise, timely and decision-oriented? Are risks discussed before they become crises? Is the management properly supported and challenged? Are conflicts of interest addressed transparently? Are shareholders engaged fairly? Does the Board evaluate its own performance and improve its work?

Corporate governance should also evolve as the company evolves. A small private company may begin with simpler but still disciplined governance practices. A family business may need clearer succession and ownership rules. A listed

company requires stronger disclosure, investor engagement and Board independence. An SOE or municipal company must combine professional commercial oversight with public accountability. A group company must ensure that group policies do not weaken the duties and judgement of subsidiary Boards. Proportionality is therefore essential, but **proportionality should never be used as an excuse for weak governance**.

Ultimately, **good governance is about trust**: trust between shareholders and the Board, between the Board and management, between the company and its employees, investors, creditors, regulators, customers and society. Trust cannot be created by formal rules alone. It is built through consistent behaviour, transparent decisions, responsible leadership and a commitment to the long-term success of the company.

This Handbook should therefore be used not only as a reference document, but as **a practical guide for continuous improvement.** Each company should periodically ask whether its governance framework is still fit for purpose, whether the Board is adding real value (and, if not, then why), and whether the company is prepared for the future. Good governance is never finished. It is a continuous journey of strengthening accountability, improving decisions and building companies that deserve confidence. Only then will the companies in the Baltics and elsewhere achieve log-term success.

ANNEXES

The following annexes accompany the Handbook. They are practical tools and examples that companies may adapt to their own circumstances; the sub-chapter in which each annex is referred to is shown in brackets.

Annex 1 Board competencies: hard and soft (sub-chapter 3.2)

Annex 2 Recommended topics for corporate governance policies (sub-chapters 1.2 and 7.4)

Annex 3 Risk categories and types (sub-chapter 5.2.3)

Annex 4 Risk register: suggested elements (sub-chapter 5.2.3)

Annex 5 Annual Board plan and Board calendar: examples (sub-chapter 6.1)

Annex 6 Board submission (cover) letter: template (sub-chapter 6.1)

Annex 7 Functions and responsibilities of the Board secretary (sub-chapter 6.5)

Annex 8 Board self-assessment questionnaire: example (sub-chapter 6.6)

Annex 9 Questionnaire for the executives: example (sub-chapter 6.6)

Annex 10 Board work improvement plan: template (sub-chapter 6.6)

ANNEX 1

BOARD COMPETENCIES: HARD AND SOFT

The hard competencies below should be covered by the Board as a whole; no individual member is expected to hold all of them. The soft competencies are expected of every Board member.

Hard competencies

COMPETENCY AREA	*KEY COMPETENCIES*
Corporate governance	Understanding of the role of the Board, fiduciary duties, Board-management relationship, committee work, conflicts of interest, independence, accountability and shareholder rights.
Industry and market knowledge	Understanding of the company's sector, customers, competitors, suppliers, market trends, regulation and key value drivers.
Strategy and business model	Ability to assess the company's strategy, business model, competitive position, growth opportunities, capital allocation and long-term value creation.
Leadership and executive experience	Practical experience of leading an organisation or a significant business unit, enabling a realistic assessment of management's plans, capabilities and execution.
Finance and accounting	Ability to read and challenge financial statements, budgets, forecasts, cash flow, capital structure, investment proposals, dividend policy and financial performance indicators.
Risk management and internal control	Understanding of risk appetite, risk registers, internal controls, assurance, compliance systems and the Board's oversight role.
Audit and assurance	Knowledge of external audit, internal audit, audit committee work, financial reporting quality, auditor independence and follow-up of audit findings.
Legal and regulatory environment	Understanding of relevant EU and national company law, securities regulation, competition law, data protection, sector-specific regulation and directors' duties.
Sustainability and ESG	Ability to oversee sustainability strategy, climate and environmental risks, social issues, stakeholder expectations, CSRD/ESRS reporting, and the integration of sustainability into business decisions.
Digital transformation and technology	Understanding of digital business models, automation, data governance, artificial intelligence, technology investments and related risks.
Cybersecurity and data protection	Ability to oversee cyber resilience, incident response, data privacy, business continuity and management's preparedness for major digital risks.
People, culture and remuneration	Ability to oversee CEO succession, senior leadership development, organisational culture, workforce issues, incentives, remuneration policy and talent risks.

COMPETENCY AREA	KEY COMPETENCIES
Stakeholder and reputation management	Understanding of how the company's decisions affect shareholders, employees, customers, regulators, communities, creditors and other stakeholders.
International and EU perspective	Awareness of cross-border governance expectations, EU regulatory developments, geopolitical risks, supply-chain issues and international market dynamics.
Crisis management and resilience	Ability to oversee management's preparation for crises, including financial stress, operational disruption, cyber incidents, reputational issues, geopolitical shocks and leadership emergencies.
Mergers, acquisitions and major transactions	Ability to assess acquisitions, disposals, partnerships, financing transactions, restructuring and integration risks.
Innovation and future trends	Ability to challenge whether the company is adapting to new technologies, changing customer expectations, sustainability transition and long-term market disruption.

Soft competencies

SOFT COMPETENCY	WHY IT MATTERS
Independent and sound judgement	Be able to think objectively and make decisions in the best interests of the company. Weigh incomplete information, assess trade-offs and make balanced decisions.
Constructive challenge	Be able to question management respectfully, without becoming operational or adversarial.
Strategic thinking	Focus on long-term direction, not only short-term results or operational details.
Integrity and ethical judgement	Act with honesty, accountability and respect for legal and ethical standards.
Courage and backbone	Be willing to raise difficult issues, challenge dominant views and speak up when needed.
Collaboration and team orientation	Be able to contribute to the Board's work without undermining collective responsibility.
Listening and openness	Listen carefully, consider different views and remain open to evidence and argument.
Communication skills	Be able to express views clearly, ask concise questions and contribute to effective discussions.
Curiosity and continuous learning	Be willing to learn about new risks, technologies, markets, regulation and stakeholder expectations.
Emotional intelligence	Understand group dynamics, manage disagreement constructively and build trust.

SOFT COMPETENCY	*WHY IT MATTERS*
Time commitment and diligence	Prepare properly, attend meetings, read materials, follow up on issues and stay informed.
Discretion and confidentiality	Handle sensitive company information responsibly.
Independence from undue influence	Avoid being captured by management, controlling shareholders, political interests or personal relationships.
Respect for the Board's role	Understand the difference between governance and management, and avoid unnecessary interference in day-to-day operations.

ANNEX 2

RECOMMENDED TOPICS FOR CORPORATE GOVERNANCE POLICIES

Each Board should decide what policies are necessary for the company in particular stage of corporate governance and business development. The list of topics provided below is indicative to get ideas for the board to consider when establishing corporate policies. Topics in bold are highly recommended.

1. **Anti-bribery and corruption prevention**
2. **Business continuity**
3. **Board nomination and selection**
4. Charities and donations
5. Community development and support
6. **Compliance**
7. **Corporate governance (defines how governance is functioning)**
8. **Conflict of interest**
9. **Diversity, equal opportunities and inclusion, Human rights**
10. **Dividends (listed, SOEs, MOEs)**
11. **Ethics, Responsible business conduct (RBC)**
12. **Fraud prevention**
13. **Information security**
14. Investment
15. **Key employees' succession**
16. **Remuneration (top executives, employees, board members)**
17. **Personal data protection, data retention**
18. **Performance evaluation of the governing bodies, individual directors and key executives**
19. **Procurement**
20. Project management oversight
21. R&D, Innovation
22. Related party transaction (may be part of a conflict of interest or ethics or other)
23. **Risk governance oversight**
24. **Safety at work, health, well-being and prevention of occupational risks**
25. **Stakeholder relationship**

26. **Supplier code of conduct**
27. **Sustainability (ESG);**
28. **Whistle-blower**
29. (for SOEs) Policy on the types of non-commercial services SOE can provide, and the rationale for provision of services and how such services are compensated
30. (for family owned) Family policies relating to family members' employment, transfer of shares, and CEO succession

ANNEX 3

RISK CATEGORIES AND TYPES

Strategic risks

1. **Corporate governance risk**
   The risk that employees will not act in the interests of shareholders and other stakeholders.

2. **Competitive risk**
   The risk of losing competitive advantage.

3. **Innovation risk**
   The risk that innovations will make your company less successful.

4. **Intellectual property risk**
   Risks related to intellectual property.

5. **Merger and acquisition risk**
   Risks related to these processes.

6. **Business risk**
   The risk that your overall business strategy and plan will be ineffective and/or fail to deliver results.

7. **Economic risk**
   The risk that the economy will enter a recession.

8. **Technological change**
   The risk that technology will become obsolete.

9. **Change management risk**
   Risks related to the management of change.

10. **Project risk**
    The risk that projects will fail (deadlines, budget).

11. **Ethics risk**
    The risk that your core principles and ethics will be breached.

12. **Reputational risk**
    The risk of damage to your company’s image.

13. **Sustainability risk**
    The risk of failing to meet sustainability goals and targets.

Financial risks

14. **Profit risk**
    The general risk that profit will decline or a loss will be incurred.

15. **Availability of capital**
    The risk that you will be unable to finance your business.

16. **Asset risk**
    Risk related to asset prices or values (for example, real estate).

17. **Interest rate risk**
    The risk that interest rates will change (rise).

18. **Currency risk**
    The risk of exchange rate changes when you buy or sell.

19. **Inflation risk**
    The risk of price increases in critical costs (for example, energy).

20. **Investment risk**
    The risk of changes in the value of investments.

21. **Liquidity risk**
    The risk that you will be unable to sell assets efficiently (quickly and at an acceptable price).

22. **Systemic risk**
    The risk that the global financial system or the national financial system will suffer a collapse.

23. **Concentration risk**
    Having one or a few dominant customers or suppliers.

24. **Credit risk**
    The risk that debtors will not repay their debts.

25. **Fraud risk**
    The risk of losses from fraud.

26. **Accounting risk**
    The risk of accounting errors.

27. **Breach of trust risk**
    The risk that your company breaches its fiduciary duties (for example, inside information).

28. **Counterparty risk**
    The risk that other companies will fail to honour their contractual obligations.

29. **Tax risk**
    The risk that your taxes will increase.

Marketing and sales risks

30. **Revenue shortfall risk**
    The general risk that revenue will decline.

31. **Demand risk**
    Lower than planned demand for your products.

32. **Market competition risk**
    The risk that competitive forces will reduce your company's revenue (for example, a price war).

33. **Sales forecast risk**
    The risk that sales forecasts will be inaccurate.

34. **New product development risk**
    The risk that new products will appear on the market.

35. **Customer relationship risk**
    The risk of damaged relationships with customers.

36. **Brand value risk**
    The risk of a decline in brand value.

37. **Publicity risk**
    The risk of negative public information.

38. **Key customer risk**
    The risk of losing a major customer.

39. **Location risk**
    The risk of choosing an unsuitable location (for example, a retail site).

Operational risks

40. **Infrastructure risk**
    Risks related to infrastructure (for example, interruption of electricity or gas supply).

41. **Maintenance and repair risk**
    Risk in the maintenance and repair process (for example, human error during equipment servicing).

42. **Product failure risk**
    The risk that your product will fail or your services will not be delivered properly.

43. **Product liability risk**
    The risk of legal liability related to your products and services.

44. **Operational quality risk**
    The general risk of operational disruption (for example, your website or e-shop is not working).

45. **Production interruption risk**
    Failure to achieve production targets.

46. **Logistics risk**
    The risk of logistics failure (for example, failure to deliver goods to your retail outlets on time).

47. **Procurement risk**
    Risk related to the purchase of goods and services.

Information technology

48. **IT architecture risk**
    The risk that the architecture of your IT systems will not meet business objectives.

49. **Data quality and data loss risk**
    The risk of poor quality data or loss of data.

50. **Technology quality risk**
    The risk of quality problems in software and hardware.

51. **Platform risk**
    The likelihood of choosing a technology platform that is unsuitable for achieving business objectives effectively.

52. **Information security risk**
    The risk of information security incidents.

People risks

53. **Employee safety risk**
    The risk that accidents will occur or that a poor working environment will affect employees and their health.

54. **Employer reputation risk**
    The risk that the company will acquire a poor reputation and find it difficult to recruit the best talent.

55. **Employer liability risk**
    The risk of a claim being brought against you for work-related actions or incidents.

56. **Employment law compliance risk**
    The risk of non-compliance with employment laws and regulations.

57. **Talent management risk**
    The risk of losing top talent and key employees.

58. **Remuneration and benefits risk**
    The risk that remuneration and benefits will be ineffective or applied inappropriately.

59. **Recruitment risk**
    The risk of hiring the wrong candidate or breaching ethics or the law in the recruitment process.

60. **Employee data privacy risk**
    The risk that you will disclose personal information about your employees.

Compliance and legal risks

61. **Compliance risk**
    The risk of failing to comply with laws and other regulations.

62. **Mandatory reporting risk**
    The risk of failing to meet regulatory reporting requirements.

63. **Liability risk**
    The risk of legal claims.

External risks

64. **Force majeure**
    Acts of nature, war and terrorism.

65. Political risk

Risk related to political change.

ANNEX 4

RISK REGISTER: SUGGESTED ELEMENTS

Important! Each company in the current status of its risk management development should set its own elements of the risk register and review them regularly.

Companies are creating an easy-to-use Excel file incorporating the following risk register elements.

I. **General information**

1. **Risk ID**. Unique identifier for each risk.
2. **Risk category.** Broad grouping (e.g., strategic, operational, financial, compliance, reputational, environmental).
3. **Risk name.** Short descriptive label.
4. **Risk description**. Detailed explanation of the risk event/scenario.
5. **Risk owner**. Person (not the name, but position) responsible for managing this risk.

II. **Risk assessment**

6. **Cause**. Why this risk exists (root cause).
7. **Potential impact**. What could happen if this risk materializes.
8. **Probability**. Rating on scale 1 to 5, where 5 is the highest probability; you should describe what means each probability (once a month, once a year, etc.)
9. **Impact**. Rating of consequences of each type of impact (e.g. impacts to company's possibilities to achieve strategic goals and objectives, health and safety, financial, environmental, business continuity. reputation).
10. **Risk level.** Result of multiplication of the probability and the highest impact rate before any risk mitigation actions are applied.

III. **Response / Mitigation**

11. **Existing risk mitigation measures.** Measures already in place to mitigate risk.
12. **Effectiveness of current mitigation**. How effective current actions are.
13. **Required mitigation action(s)**. Specific activities to manage the risk in order to reduce it.
14. **Owner of the action(s)**. Employee (position) who is responsible for mitigation actions.

15. **Action(s) deadline**. Deadline for risk mitigation action.

IV. **Monitoring and Reporting**

16. **Last updated.** When this risk was last reviewed.
17. **Reporting line.** To whom this risk management should be reported to (e.g. board, risk committee, top management)

ANNEX 5

ANNUAL BOARD PLAN AND BOARD CALENDAR: EXAMPLES

This annex gives an example of an annual Board calendar for a company whose Board meets every month. However, each Board has to make decision on the appropriate number of the meetings it wants to plan for a year. It will depend on the company type (e.g. private or listed; regulated or not) complexity of its operations and many other factors. It combines the two formats commonly used in practice: a meeting-by-meeting plan, which shows the focus and the main items of each meeting, and a calendar matrix, which shows in which months each recurring activity of the Board takes place. The example assumes a financial year equal to the calendar year, an annual general meeting in April, quarterly reporting and three committees (audit, remuneration and nomination). The wording is neutral and can be used by a one-tier Board or by a Supervisory Board (also called the Council). Companies should adapt the calendar to their own size, ownership, reporting cycle and regulatory requirements; a Board that meets less often can merge adjacent meetings.

Standing items at every meeting are not repeated in the tables: approval of the agenda and of the minutes of the previous meeting, follow-up of decisions taken, the CEO's report on business performance and key events, the financial report against budget, the risk and compliance dashboard, reports of the committee chairs and a private Board-only session without management at the end of each meeting.

Important: items in the calendar are for illustration only and should not be understood as the best governance practice.

1. Meeting-by-meeting plan

MONTH	FOCUS OF THE MEETING	MAIN ITEMS AND EXPECTED BOARD OUTCOME (DECISION / DISCUSSION / MONITORING), IN ADDITION TO THE STANDING ITEMS
January	Start of the year	– Preliminary (unaudited) results of the previous year; outlook for the year – Principal and emerging risks for the year; review of risk appetite – Review of the Board's annual plan and areas of focus

MONTH	FOCUS OF THE MEETING	MAIN ITEMS AND EXPECTED BOARD OUTCOME (DECISION / DISCUSSION / MONITORING), IN ADDITION TO THE STANDING ITEMS
February	Full-year results and Board effectiveness	– Full-year results as presented by management; draft annual report – Full-year performance assessment of the CEO; variable pay outcomes – Results of the Board and committee evaluation; improvement action plan – Review of committee composition and charters
March	Annual accounts and convening the AGM	– Review and, where within the Board's authority, approval of the audited financial statements, management report and sustainability statement – External auditor's report and independence; annual review of the effectiveness of the risk management and internal control framework – Profit distribution and dividend proposal – Corporate governance statement and remuneration report – Convening the annual general meeting: agenda, resolutions, candidates
April	Annual general meeting	– Annual general meeting; Board's dialogue with shareholders and key stakeholders – Constitution of committees after the meeting; induction of new members – First-quarter trading update – Investor feedback and investor relations plan
May	First quarter and risk	– Approval of the first-quarter interim report (if required) – Risk register review; compliance and whistleblowing report – Deep dive: business unit or subsidiary 1 – Health, safety and environment review
June	Strategy review – part one	– Market, competition, technology and regulatory developments; progress against strategic objectives – Strategic risks and scenarios; resilience and business continuity – Sustainability strategy and targets – Capital structure, financing and dividend policy review
July	Mid-year check (may be held virtually)	– Full-year forecast; major projects and transactions – Deep dive: cybersecurity, IT, data and AI governance, and digital transformation – Deep dive: business unit or subsidiary 2 – Identification of strategic choices and issues for the September strategy session

MONTH	FOCUS OF THE MEETING	MAIN ITEMS AND EXPECTED BOARD OUTCOME (DECISION / DISCUSSION / MONITORING), IN ADDITION TO THE STANDING ITEMS
August	Half-year results	– Approval of the half-year interim report – Half-year risk, compliance and internal audit reports – Half-year assessment of the CEO's performance – Review of material related party transactions and conflicts of interest; confirmation of related controls and disclosures – Follow-up of the Board improvement action plan
September	Strategy session (off-site) – part two	– Approval of the updated strategy and the three-year plan, including investments, acquisitions and divestments – Innovation, research and development, technology priorities – People and culture: talent review, engagement, tone at the top – Succession planning for the CEO and executives; separate review of Board succession and future competence needs
October	Third quarter and policies	– Third-quarter trading update; budget guidelines and assumptions for the next year – Review of key policies: risk management, compliance, code of conduct, delegation of authority – Evaluation of the external auditor; recommendation on (re)appointment – Deep dive: business unit or subsidiary 3
November	Third quarter and budget	– Approval of the third-quarter interim report – Draft budget and investment plan; financing needs – Risk assessment for the next year; insurance cover, including D&O – Remuneration policy review; stakeholder engagement review
December	Budget and governance for the next year	– Approval of the budget, risk appetite for the next year, KPIs and variable pay targets – Objectives and KPIs of the CEO and the executive team – Board annual plan, committee work plans and meeting calendar for the next year; approval of the internal audit plan for the next year – Launch of the Board and committee evaluation – Compliance with the corporate governance code; Board and committee charters

2. Calendar matrix: activities by month

A dot marks the month in which the activity is on the Board's agenda. Committees meet one to two weeks before the Board meeting for which they prepare recommendations.

This matrix is for indicative purposes only and should not be understood as the best practice

ACTIVITY	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC
1. MEETING SCHEDULE												
Board meeting	●	●	●	●	●	●	●	●	●	●	●	●
Strategy session (off-site)									●			
Annual general meeting				●								
Audit committee	●	●	●		●			●		●	●	
Remuneration committee	●	●									●	●
Nomination committee		●	●						●			●
Board-only session without management				●				●				●
2. Strategy and budget												
Strategy review (part one)						●						
Approval of strategy and three-year plan									●			
Capital structure and financing review						●						
Budget guidelines and assumptions										●		
Draft budget and investment plan											●	
Approval of budget and KPIs												●
3. Strategy implementation and deep dives												
Progress against strategic objectives			●			●			●			●
Deep dive: business unit or subsidiary					●		●			●		
Deep dive: market outlook / investor relations	●			●								
Deep dive: cybersecurity, IT and digital							●					
Deep dive: sustainability						●						

ACTIVITY	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC
1. MEETING SCHEDULE												
Major projects and transactions							•				•	
4. CEO and executive team												
Objectives and KPIs approved	•											
Half-year performance assessment								•				
Full-year performance assessment		•										
Variable pay outcomes / targets		•										•
Remuneration policy review											•	
Succession planning and talent review									•			
5. Financial reporting and accountability												
Preliminary full-year results	•											
Full-year results and draft annual report		•										
Audited financial statements and annual report approved			•									
Dividend proposal			•									
Quarterly and half-year interim reports					•			•			•	
Full-year forecast							•			•		
6. Risk, control and compliance												
Risk appetite and key risks	•											
Risk register review; risk assessment for next year					•						•	

ACTIVITY	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC
1. MEETING SCHEDULE												
Internal audit plan / reports	●	●						●				
Compliance and whistleblowing reports					●			●			●	
Related party transactions review								●				
External auditor: report / evaluation			●							●		
Insurance cover, including D&O											●	
7. Policies and governance documents												
Board charter and committee charters												●
Delegation of authority										●		
Risk management and compliance policies; code of conduct										●		
Remuneration policy											●	
Corporate governance code compliance			●									●
8. Board effectiveness												
Board and committee evaluation: launch / results / follow-up		●						●				●
Committee composition and charters reviewed		●		●								
Induction of new members				●								
Board training or site visit					●					●		
Board annual plan and calendar for next year												●

ACTIVITY	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC
1. MEETING SCHEDULE												
9. Shareholders and stakeholders												
Convening the AGM: notice and documents			•									
Dialogue with shareholders / investor feedback				•						•		
Report to owners on Board evaluation (where applicable)				•								
Stakeholder engagement review											•	

The matrix is a planning tool for the Chair and the Board secretary: once filled in, it shows at a glance whether every matter reserved to the Board has its place in the year, whether the workload is evenly spread and whether the Board leaves enough time for strategy and forward-looking topics. It should be reviewed after the Board evaluation and approved, together with the meeting dates, at the last meeting of the preceding year.

ANNEX 6

BOARD SUBMISSION (COVER) LETTER: TEMPLATE

Company "XXX"

Form for submitting an item for consideration at a Board meeting

The form below is an example. Where necessary, the persons preparing a submission may add other sections at their discretion, depending on the nature of the item under consideration. The right-hand column explains what each section should contain; in a completed submission it is replaced by the actual content.

NO.	SECTION OF THE SUBMISSION	WHAT TO INCLUDE
1.	**Date**	Date of preparation of the submission (not the date of the meeting).
2.	**Agenda item**	The agenda item as worded in the agenda (copied from it). The item number is not given.
3.	**Legal basis**	The specific article of the law, the articles of association, a policy or another document under which the item is submitted to the Board meeting (the provisions are quoted). This part is agreed with the Board secretary and, where necessary, with the company's lawyer.
4.	**Type of item**	Possible types: – for decision (items on which the Board has to take a decision); – for discussion (where no decision is planned at the meeting); – for information (reports and other matters).
5.	**Essence of the item**	A short and clear statement (at most three or four sentences) of what decision is proposed and why (what the problem is, what change is sought and similar). Examples: (i) the Board is asked to decide on the construction of a plant (details) at a cost of EUR x; the new plant will increase production volumes (details), bringing the company EUR x of additional revenue per year; (ii) a draft policy is submitted to the Board for approval in a new wording, taking into account that <…>.

NO.	SECTION OF THE SUBMISSION	WHAT TO INCLUDE
6.	**Rationale for the proposed decision**	A detailed statement of the facts and of the reasons why the decision proposed to the Board is in the best interests of the company (preferable no longer than 10 pages) If several alternatives are presented, management must clearly identify which alternative the Board is asked to vote on and why. Where an item is submitted for decision, this section must contain enough information and reasoning for the Board to understand the consequences of taking or not taking the decision and to take an informed decision, satisfied that it is in the best interests of the company. The text may be structured freely, as long as the information is presented clearly. The rationale usually has two parts: – factual information (objective data): – context (for example, changes in legislation that require the Board to change the company's activities); – background (excluding the information given under item 7, "Link with previous decisions and recommendations"); – where a document or transaction is submitted for approval, a summary of its main terms; – assessment of the facts, analysis and conclusions (the subjective part), for example: – why the proposed decision should be taken; – the consequences of the decision; – the possible options, with their advantages and disadvantages (for example, where the acquisition of an asset is proposed, the alternatives of leasing or building it); – where several options are possible, the grounds for the option proposed by management. Where more detailed information is needed, the text of the submission should not be overloaded; the additional information is attached as annexes. Where opinions of external advisers have been obtained, they are referred to in this section; the full opinions may be attached as an annex.
7.	**Alignment with strategy**	The submission should explain how the proposed decision aligns with the company's strategy and/or business plan.
8.	**Risks and management measures**	The submission should indicate the key risks and their levels associated with the proposed decision and the proposed measures to manage them.
97.	**Link with previous decisions and recommendations**	The specific Board decision, or the proposals or recommendations of its committees, relating to the item, with the date of the meeting; the decision or recommendation is not only referred to but quoted. This part is agreed with the Board secretary.
108.	**Proposed decisions**	The decision proposed to the Board. The resolution must be short, clear and unambiguous. Where information that is missing for the decision will be obtained only at the meeting, a recommendation on the decision may be given instead.

NO.	SECTION OF THE SUBMISSION	WHAT TO INCLUDE
119.	**Opinion of the Board secretary**	An opinion on whether the item falls within the competence of the Board and whether the proposed decision is consistent with previous Board decisions and assignments and with the proposals and recommendations of its committees. *Position, name and surname* _____ *(signature)*
1210.	**Financial opinion**	A short opinion on (i) the financial consequences of the proposed decision and when they will arise; and (ii) whether the expenditure is planned in the budget and under which budget line. Where financial information is given in the rationale, only a summary is provided here (no repetition). Where more detailed information is needed to explain the financial consequences, an annex with the additional information is attached. *Position, name and surname* _____ *(signature)*
1311.	**Legal opinion**	An opinion on whether the proposed decision complies with the applicable laws and the company's internal documents. Where certain requirements are not fully met, an explanation is given. The legal basis given elsewhere in the submission is not repeated; a summary is provided. *Position, name and surname* _____ *(signature)*
1412.	**Endorsements**	The persons with whom the submission has been agreed, depending on its content. These may be any stakeholders, as well as the senior or functional managers whose areas are affected. When endorsing, each person states why they recommend the proposed decision. The submission is also signed by the person who prepared it. I recommend that the decision be taken because … *Position, name and surname* _____ *(signature)* Person who prepared the submission *Position, name and surname* _____ *(signature)*
1513.	**Person initiating the item**	Usually, the CEO. *Position, name and surname* _____ *(signature)*
1614.	**Person presenting the item**	The person (position, name and surname) who will present the item at the meeting.
1715.	**Annexes**	The annexes attached to the submission, numbered. The annexes form part of the submission, so the persons signing it give their opinions on the annexes as well.

ANNEX 7

FUNCTIONS AND RESPONSIBILITIES OF THE BOARD SECRETARY

The Board secretary plays a very important role in the governance and administration of a company. The secretary's main function is to ensure that the Board works effectively and complies with legal and regulatory requirements. The main functions and duties of the Board secretary are set out below.

1. **Support for Board meetings**

   – Planning and organising the meetings of the Board and its committees.
   – Preparing and distributing notices of meetings, agendas and supporting materials.
   – Coordinating the logistics of meetings, including the venue, technology and, where needed, catering.
   – Taking the minutes of Board meetings and keeping the minutes of all meetings.

2. **Ensuring good governance practice**

   – Ensuring that the company's governance practices comply with the applicable laws, regulations and the articles of association.
   – Informing the Board of changes in governance requirements and best practice and of new developments.
   – Helping the Board to maintain an effective corporate governance system.

3. **Fiduciary duties of Board members**

   – Helping the Board to understand and fulfil its fiduciary duties, including the duties of loyalty and care.
   – Advising on the legal duties and ethical obligations of Board members.

4. **Management of corporate documents**

   – Maintaining and safeguarding the company's documents, including the articles of association, governance documents, Board meeting materials and Board resolutions.
   – Safeguarding other important corporate documents and records.

5. **Compliance and reporting**

- Ensuring that the company complies with all legal and regulatory requirements, including annual reporting and disclosure.
- Informing the Board of changes in laws, regulations and governance practice and advising the Board on these matters.
- Helping to prepare and submit the reports required by regulatory authorities.

6. **Support for Board communication**

- Acting as the link between the Board and the CEO and the executive team.
- Helping to maintain communication between Board members, shareholders and other stakeholders.

7. **Induction and development of Board members**

- Supporting new Board members by providing them with the essential information about the company, its governance and their roles and responsibilities (induction).
- Organising training and professional development for Board members where needed.

8. **Management of conflicts of interest**

- Helping to identify and manage the conflicts of interest of Board members and senior executives.
- Helping to develop and implement the conflict of interest policy.

9. **Board evaluation and improvement of Board work**

- Helping the Board to carry out its evaluation and to improve its work.
- Helping to collect and analyse feedback in order to increase the effectiveness of the Board.

10. **Administration of the secretary's office**

- Managing the administrative matters of the company secretary's office, including budgeting, recruitment and the allocation of resources.
- Maintaining an effective and well-organised document management system.

The Board secretary is the key person ensuring the transparency and accountability of the company's activities and effective good governance within the company. The secretary helps to maintain the integrity of the Board's actions and promotes the confidence of shareholders and stakeholders. The specific duties may differ

depending on the size of the organisation, its industry and the applicable legal requirements.

ANNEX 8

BOARD SELF-ASSESSMENT QUESTIONNAIRE: EXAMPLE

Company: _____ Assessment date: _____

Board member (first name and surname): _____

For each statement, enter your score in the appropriate column (1–5), not a cross: 1 – definitely not; 2 – not quite; 3 – neutral / do not know; 4 – yes, in principle; 5 – yes, without a doubt. Add comments where useful.

STATEMENT	1	2	3	4	5	COMMENTS
1. General approach, composition of the Board						
1.1. The Board has a clear understanding of the expectations of all shareholders of the company.						
1.2. The Board has reviewed and set the Company's strategy, responding to shareholder expectations, the national and EU regulatory environment, and the trends in this industry						
1.3. The Board has a clear understanding of the Company's long-term and medium-term priorities.						
1.4. Cooperation between the Board and the Company's CEO is constructive.						
1.5. The Board is appropriately involved in maintaining relationships with key stakeholders.						
1.6. The Board has considered the need for Board committees and ensured that the necessary committees are established.						
1.7. The Board committees operate effectively.						
1.8. The Board properly oversees the matters delegated to the committees and ensures that the delegated tasks are properly managed and that each committee duly reports to the Board.						
1.9. The size of the Board is appropriate						
1.10. The diversity of the Board is appropriate						
1.11. The composition of the Board, in terms of the skills and experience of its members, is balanced.						

STATEMENT	1	2	3	4	5	COMMENTS
1.12. The Board has the necessary diversity of competences and qualifications in governance-related matters, for example in corporate finance, strategic planning, risk management, organisational development, human resources, compliance and other areas.						
1.13. The duties of the Board are fully and clearly defined in the company's articles of association and internal regulations.						
1.14. The governance framework (policies, codes and similar documents) is up to date and appropriate for overseeing the company's activities						
Average score						
Additional comments:						
2. Role and duties of the Board						
2.1. The Board has a clear understanding of the Board's role and duties in the Company.						
2.2. The Board effectively combines its supervisory and strategic leadership functions.						
2.3. The Board gives sufficient consideration to the long-term business strategy and regularly monitors its implementation.						
2.4. The Board approves the Company's annual budget and reviews its assumptions.						
2.5. The Board sets key performance indicators (KPIs) based on the SMART principle and monitors their achievement.						
2.6. The Board effectively oversees the financial position and the effectiveness of financial controls.						
2.7. The Board regularly oversees risk management and ensures its effectiveness.						
2.8. The Board ensures that a reliable internal control and compliance system is in place in the Company.						
2.9. The Board ensures the independence, effectiveness and high professional standard of internal audit.						
2.10. The Board communicates sufficiently with the external auditors.						
2.11. The Board oversees the Company's communication activities.						

STATEMENT	1	2	3	4	5	COMMENTS
2.12. The Board takes leadership in the area of sustainability.						
2.13. The Board continuously reviews and improves the Company's governance framework and practices.						
Average score						
Additional comments:						
3. Board meetings						
3.1. The Board's work is planned in advance; it has an annual calendar of meetings with preliminary agendas.						
3.2. The Board meets sufficiently often to be able to properly oversee the activities of the Company and management and to perform its duties.						
3.3. The duration of Board meetings is sufficient for meaningful discussion and effective decision-making.						
3.4. In most Board meetings, members participate in person (not remotely).						
3.5. All Board members regularly attend Board meetings.						
3.6. The agenda and materials are provided to the Board sufficiently in advance of the meeting.						
3.7. The documents submitted for Board meetings are of good quality and enable members to discuss properly and take decisions.						
3.8. The agendas balance strategy implementation, performance reviews, controls, projects and other matters.						
3.9. Strategic and forward-looking matters take up most of the time on the agendas; there are no matters of an operational nature						
3.10. Matters on which the Board must take a decision are clearly identified and presented in sufficient detail and in an informative manner.						
3.11. Board meetings keep to the agenda and to the time allocated to its items.						
3.12. Independent Board members participate in taking all Board decisions.						
3.13. Board members are active and effective, i.e. they attend meetings, are well prepared, discuss constructively and are decisive.						

STATEMENT	1	2	3	4	5	COMMENTS
3.14. Board decisions are always confirmed in well-written and clear minutes of meetings (including the substantive questions and answers and the main arguments).						
3.15. Minutes are prepared promptly after each Board meeting, and each Board member reviews them in good time (and, where necessary, submits comments); all comments are duly taken into account.						
3.16. The Board effectively monitors the implementation of its decisions and assignments.						
Average score						
Additional comments:						
4. Board working culture						
4.1. The Board clearly understands and agrees with the Company's purpose, vision, mission, goals and/or objectives, and values.						
4.2. The Board performs its duties as a motivated and well-functioning team.						
4.3. All Board members can express their opinions freely.						
4.4. Board discussions are challenging and constructive, without micromanagement.						
4.5. The atmosphere inspires trust and helps generate new ideas.						
4.6. The Board encourages diversity of thinking and understands the dangers of groupthink.						
4.7. The Board pays attention to conflicts of interest and does not consider that the shareholders who appoint Board members exert undue influence on the Board members they have appointed.						
4.8. The Board considers that all Board members give priority to the interests of the Company and all shareholders, rather than to the interests of the shareholders who appointed them or of other stakeholders.						
4.9. The Board does not tolerate corruption or fraud.						
4.10. In taking decisions, the Board is guided by the Company's values and ethical principles.						

STATEMENT	1	2	3	4	5	COMMENTS
4.11. The Board maintains a culture of lifelong learning and knowledge renewal, and provides sufficient support for the continuous training and education of Board members and employees.						
4.12. The Board takes leadership in shaping the organisation's culture.						
Average score						
Additional comments:						
5. Chair of the Board						
5.1. The duties of the Chair of the Board are clear to all Board members.						
5.2. The Chair of the Board communicates appropriately with all Board members.						
5.3. The Chair of the Board communicates sufficiently with stakeholders and duly informs all Board members about this.						
5.4. The Board discusses the role and duties of the Chair of the Board.						
5.5. The Chair of the Board is well prepared for Board meetings.						
5.6. The Chair of the Board ensures that, during meetings, the Board concentrates on strategic matters						
5.7. The Chair of the Board helps the Board keep to the agenda and to the time allocated for discussing its items.						
5.8. The Chair of the Board ensures that every Board member has the opportunity to be heard.						
5.9. The Chair of the Board is able to manage differing views among Board members.						
5.10. The Chair of the Board can be firm with the Board members as a group when their discussions go off track.						
5.11. The Chair of the Board knows how to communicate directly with an individual Board member when that member's behaviour needs to change.						
5.12. The Chair of the Board helps the Board work together smoothly.						
5.13. The Chair of the Board has good listening skills.						

STATEMENT	1	2	3	4	5	COMMENTS
5.14. The Chair of the Board delegates responsibility to Board members effectively.						
5.15. The decisions of the Chair of the Board are supported by the Board members.						
5.16. The Chair of the Board maintains a constructive and professional relationship with the Company's CEO.						
Average score						
Additional comments:						
6. Cooperation between the Board and the Company's CEO						
6.1. The Board provides the CEO with clear expectations and guidance and indicates clear directions for work.						
6.2. Communication between the Board and the Company's CEO is productive, transparent and two-way.						
6.3. Board members understand the boundaries of responsibility between the Board and the Company's CEO.						
6.4. The Board trusts the decisions of the Company's CEO.						
6.5. The Board assesses the Company's CEO primarily on the achievement of the strategic goals set for the Company; the assessment process is clear and professional						
6.6. The CEO feels supported by the Board, while being sufficiently and appropriately challenged.						
6.7. The Board and its individual members do not interfere in the CEO's day-to-day activities						
Average score						
Additional comments:						
7. Individual self-assessment						
You have:						
7.1. The information needed to take decisions on the items on the Board meeting agenda, including the opportunity to ask questions and receive answers.						
7.2. Experience of, an understanding of, and an interest in the work of the Board and good governance practices.						

STATEMENT	1	2	3	4	5	COMMENTS
7.3. The courage and standing to express your opinion independently, even if it may differ from that of other Board members, the shareholder(s) and management, and your opinion is heard.						
7.4. Commitment, leadership and initiative in building a strong and effective management team for the Company.						
7.5. The competences and qualifications needed to carry out the tasks entrusted to you.						
7.6. Sufficient knowledge of the laws and regulations applicable to the functions and duties of Board members.						
7.7. The ability to listen to and cooperate with the Company's CEO and other Board members.						
7.8. Confidence in the preparedness of the Board committees and in their recommendations to the Board.						
7.9. A clear understanding of your fiduciary duties to the Company.						
7.10. Time to prepare for and contribute effectively to the work of the Board.						
7.11. Experience and knowledge enabling you to assess the company's performance.						
7.12. Sufficient knowledge of finance for the work of a Board member.						
7.13. Sufficient knowledge of strategic planning for the work of a Board member.						
7.14. Sufficient knowledge of corporate governance for the work of a Board member.						
7.15. Sufficient knowledge of risk management for the work of a Board member.						
7.16. Sufficient knowledge of organisational development for the work of a Board member.						
7.17. Sufficient knowledge of the sector in which the Company operates for the work of a Board member.						
7.18. Sufficient knowledge of digitalisation for the work of a Board member.						
7.19. Sufficient knowledge of cyber security for the work of a Board member.						

STATEMENT	1	2	3	4	5	COMMENTS
7.20. Sufficient knowledge of sustainability for the work of a Board member.						
Average score						
Additional comments:						
8. Any other comments, suggestions or observations of the Board member						
1.						
2.						
3.						

ANNEX 9

QUESTIONNAIRE FOR THE EXECUTIVES: EXAMPLE

Dear executives,

As part of its annual self-evaluation, the Board requests your structured and candid feedback on its performance, behaviours, and ways of working.

Purpose of your input

The primary purpose of this input is to help the Board improve its work by providing the executive perspective on:

- How the Board's actions and processes are experienced by leadership;
- How effectively the Board supports the organization's strategy and long-term objectives;
- How the Board could bring even more value into interaction with CEO and other executives.

It is not about the judgement, but about higher efficiency of the Board and better Board-CEO-executives interaction that will improve the whole organisation.

Call to action

Please provide open and balanced input, highlighting both strengths and areas for improvement. This process is crucial for strengthening alignment, trust, and effectiveness between the Board and executives, benefiting the entire organization.

The Board thanks you for your contribution to strengthening the organization's governance and leadership.

Questionnaire

Score each question from 1 (lowest) to 5 (highest) and add your answer or comment. Open questions are answered in the last column only.

NO.	QUESTION	SCORE (1–5)	ANSWER / COMMENTS
1. Board–management interaction & dynamics			
1.1	How effectively does the Board engage with management during meetings?		

NO.	QUESTION	SCORE (1–5)	ANSWER / COMMENTS
1.2	How well does the Board create a constructive and respectful environment for open dialogue?		
1.3	How well does the Board demonstrate trust in management while still exercising appropriate oversight?		
1.4	How well Board discussions are focused, disciplined, and free from micromanagement?		
1.5	How well does the Board sufficiently take into account management's expertise and perspectives when making decisions?		
1.6	How well does the Board foster an inclusive environment where all directors and executives contribute?		
2. Strategic oversight & long-term focus			
2.1	To what extent does the Board provide clear strategic direction while allowing management to execute?		
2.2	To what extent does the Board focus on long-term priorities rather than operational matters?		
2.3	To what extent does the Board support management in addressing strategic risks and opportunities?		
2.4	To what extent is the Board forward-looking in terms of market trends, technology, HR/people issues, sustainability, and governance topics?		
3. Quality of challenge & constructive feedback			
3.1	How well does the Board provide constructive strategic challenge that improves the quality of decision-making?		
3.2	To what extent Board members ask relevant, well-prepared, and value-adding questions?		
3.3	How well does the Board demonstrate that it holds management accountable in a consistent and unbiased manner?		
3.4	How well does the Board balance its support and challenge?		
4. Communication, quality of information flow			
4.1	To what extent the Board's request for information is clear, reasonable, and aligned with its governance responsibilities?		

NO.	QUESTION	SCORE (1–5)	ANSWER / COMMENTS
4.2	To what extent the Board and/or Chairperson is clearly communicating requirements about the Board meeting materials (depth, content, details) to make them appropriate and helpful for the Board to hold efficient discussion and make required decisions?		
4.3	How well does the Board make efficient use of the information provided by management (presentations, KPIs, dashboards, risk reports, etc.)?		
4.4	In your opinion how effective is communication between the Board (or its committees) and management (i.e. clear, respectful, and open)?		
4.5	To what extent is the Board prepared to provide effective oversight and support during a major crisis or disruption?		
5. Chairperson's performance and value added			
5.1	How effective is the Chair in leading the Board and setting the agenda?		
5.2	To what extent division of responsibilities between the Chair (governance) and the CEO (management) is clear and respected by both parties?		
5.3	To what extent Chair interacts with management (outside of the CEO) in a way that supports the CEO's authority and avoids micromanagement?		
5.4	To what extent Chair and CEO are aligned on the company's strategic priorities, providing a stable and consistent direction for the management team?		
5.5	To what extent does the Chair–CEO relationship enable a balanced leadership challenge that translates Board expectations into clear direction for the CEO and management?		
5.6	To what extent partnership between the Chair and CEO demonstrates a high degree of mutual respect and trust?		
5.7	To what extent does the relationship between the Chair and CEO contribute positively to the overall tone and culture of the company?		
5.8	What is one specific area where improved collaboration or clarity between the Chair and CEO would most enhance management team effectiveness?		

NO.	QUESTION	SCORE (1–5)	ANSWER / COMMENTS
5.9	Are there any instances where you believe the Chair-CEO dynamic has negatively affected management's ability to execute strategy? (Please describe without naming individuals.)		
6. Board processes & meeting effectiveness			
6.1	To what extent are the Board meetings well-structured to enable effective discussion and decisions?		
6.2	How well does the Board allocate sufficient time to strategic items vs. administrative or operational issues?		
6.3	To what extent decisions are made in a timely and decisive manner, they are not postponed?		
6.4	How well does the Board follow up on decisions and action items clearly and consistently?		
6.5	How well does the Board demonstrate strong internal discipline (preparation, agenda discipline, confidentiality, etc.)?		
7. Competence, composition & skills of the Board			
7.1	To what extent does the Board have the right mix of competencies required for current and future challenges?		
7.2	How well do Board members demonstrate adequate understanding of the company’s business and industry?		
7.3	How do you feel to what extent the Board is open to external perspectives and continuous learning?		
8. Interaction with the CEO specifically			
8.1	How well does the Board provide the CEO with clear expectations and constructive guidance?		
8.2	How well does the Board support the CEO in addressing key challenges (strategy, leadership, talent, transformation, risk, etc.)?		
8.3	To what extent is the CEO evaluation process by the Board fair, transparent, consistent and is it creating maximum value for the CEO?		
8.4	How well does the Board and Chairperson support and advise the CEO to develop his competences and performance?		

NO.	QUESTION	SCORE (1–5)	ANSWER / COMMENTS
9. Interaction with broader management team			
9.1	How well do Board members show respect and professionalism in interactions with senior management?		
9.2	How well do Board members listen carefully to management presentations and engage meaningfully?		
9.3	How well does the Board provide an opportunity for management to share concerns or insights openly?		
9.4	To what extent the Board understands the realities of day-to-day operations without overstepping boundaries of management work?		
10. Risk, compliance & governance oversight			
10.1	How effectively does the Board oversee risk management and internal controls?		
10.2	How well does the Board sufficiently consider sustainability, ESG, and reputational risks?		
10.3	How effectively does the Board monitor the company's engagement with its key non-shareholder stakeholders?		
10.4	To what extent are the processes of governance and their purposes used by the Board clear to management?		
11. Board committee(s)			
11.1	How effective is the Board committee(s) in interacting with management?		
11.2	To what extent Board committee(s) requests are reasonable and aligned with its mandate?		
11.3	How well does the Board committee(s) operate professionally, with clear communication back to the Board and management?		
12. Overall performance & suggestions			
12.1	What could the Board do in order to improve the value it creates even more?		
12.2	What behaviours or processes should the Board improve to work more effectively with management?		

NO.	QUESTION	SCORE (1–5)	ANSWER / COMMENTS
12.3	Is there anything the Board should stop doing because it does not add value?		
12.4	Additional comments or suggestions.		

ANNEX 10

BOARD WORK IMPROVEMENT PLAN: TEMPLATE

Company "XXX" Board performance improvement plan for the year 20xx

Date of preparation: _____

NO.	AREA FOR IMPROVEMENT	PROPOSALS FOR IMPROVEMENT	DEADLINE	RESPONSIBLE PERSON
1.	BOARD COMPETENCE			
1.1				
1.2				
2.	CORE AREAS OF BOARD FOCUS			
2.1				
2.2				
3.	BOARD MEETINGS			
3.1				
3.2.				
4.	WORK OF THE BOARD CHAIR			
4.1				
4.2				
5.	OTHER IMPROVEMENTS [enter the required area]			
5.1				
5.2				

Signature of the Board Chair: _____ Date: _____

SOURCES AND FURTHER READING

List of the corporate governance and related documents mentioned in the Handbook

1. OECD G20 Principles of Corporate Governance
2. EC: 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
3. International Finance Corporation **Corporate Governance Methodology**
4. The Corporate Governance Code for the Companies Listed on Nasdaq Tallinn
5. Good Corporate Governance Recommendations for Companies in Latvia
6. The Corporate Governance Code for the Companies Listed on Nasdaq Vilnius
7. ESG Guidelines for Baltic Boards – What, Why, and How https://www.bicg.eu/wp-content/uploads/2022/09/ESG-Guidelines-for-Baltic-Boards.pdf
8. ESG Governance: questions boards should ask to lead the sustainability transition https://www.bicg.eu/wp-content/uploads/2024/01/ESG-Governance-toolkit-for-boards_FINAL-1.pdf
9. A Practical Guide for Boards and Leadership Teams on Sustainability https://www.bicg.eu/wp-content/uploads/2022/01/A-practical-guide-for-boards-leadership-teams-on-sustainability-11.pdf
10. Cyber-Risk Oversight - Key Principles and Practical Guidance for Corporate Boards in Europe" https://www.bicg.eu/wp-content/uploads/2020/09/Handbook-1.pdf
11. https://practicalrisktraining.com/iso31000
12. https://pecb.com/whitepaper/iso-31000-risk-management--principles-and-guidelines
13. COSO Enterprise Risk Management – Integrated Framework, 2017
14. https://www.theiia.org/en/standards/2024-standards/global-internal-audit-standards/
15. BOARD EVALUATION RECOMMENDATIONS FROM ECODA https://www.bicg.eu/wp-content/uploads/2025/07/20250617-ecoDa-Board-Evaluation-Recommendations.pdf
16. G20/OECD Principles of Corporate Governance (2023) https://www.oecd.org/content/dam/oecd/en/publications/reports/2023/09/g20-oecd-principles-of-corporate-governance-2023_60836fcb/ed750b30-en.pdf

ABOUT THE AUTHORS

This Handbook draws on decades of hands-on corporate governance experience of the co-authors in private, listed, state-owned and municipal companies across the Baltic region. They are senior practitioners, who have served as Board members, Chairs, Audit Committee members and Corporate Secretaries, led legal functions at major Baltic companies and law firms. Their expertise covers corporate governance, investor relations and sustainability, M&A, shareholder disputes, restructuring and insolvency, organisational culture, etc. The Handbook was also reviewed by corporate governance experts in Latvia and Estonia, so it applies across all three Baltic countries.

Agnė Jonaitytė

Partner, NOOR law office

Agnė has more than 18 years of experience in finance law and corporate governance. She also brings an issuer's view of capital markets, as she was a Management Board member responsible for corporate governance, investor relations and sustainability at a Vilnius and Warsaw dual listed company. Agnė has extensive experience as a Corporate Secretary serving listed entities, financial institutions and other companies.

LINKEDIN

Gediminas Varnas

President and member of the Management Board at Nasdaq Vilnius

Gediminas has more than 20 years of experience in the Baltic capital market, specialising in capital market law and corporate governance. Alongside his professional work, he has lectured on business law at Vilnius University for many years.

LINKEDIN

Povilas Žukauskas

Partner, WALLESS law firm

For over 20 years, Povilas has advised shareholders, Boards and management on M&A, shareholder disputes, corporate governance, as well as restructuring and insolvency. His practice covers the key moments in a company's life, from deals and growth to conflicts between shareholders as well as financial difficulties.

LINKEDIN

Renata Damanskytė-Rekašienė

Head of Legal, Miesto gijos

Renata has 18 years of experience in commercial law and corporate governance, with a career spanning private practice at a leading Lithuanian law firm as well as the leadership of in-house legal functions at large corporate groups in the energy and retail sectors.

LINKEDIN

Rytis Ambrazevičius

Board member at ecoDa, President of the BICG, independent Board member and Chair of Audit, Risk and Sustainability Committee at Vilniaus vandenys

Rytis brings 15 years of experience serving as an independent Board member and Chair across state-owned, municipal, private, and listed companies, advancing corporate governance standards both regionally and at the European level.

LINKEDIN

Simona Grinevičienė

Chief Operational Officer, EPSO-G; member of the BICG Board

Simona has more than 20 years of experience in leadership, corporate governance and legal roles across the energy, financial services and public sectors. She chairs the Board of Baltpool and serves as an independent member of the Supervisory Board and Audit Committee at the European Merchant Bank.

LINKEDIN