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ΕΛΛΗΝΙΚΟ ΠΑΡΑΤΗΡΗΤΗΡΙΟ ΕΤΑΙΡΙΚΗΣ ΔΙΑΚΥΒΕΡΝΗΣΗΣ

Audit and Risk Committees in Greece: Insights from the ESG Index

Legislative Framework and the Greek Corporate Governance Code

With the recent Law 4706/2020 (*Corporate Governance Law* or *Law*) and the parallel repeal of the relevant articles of Law 3016/2002, the modernization of the legislative framework for corporate governance of joint-stock companies is sought, as well as the clarification of pressing issues pertinent to legal practice and theory.

By Article 17 of the Law, companies should adopt a corporate governance code, which has been issued by a reputable body. Subsequently, the regulation provides for a general authorization to the Hellenic Capital Market Commission (HCMC) to determine any specific matter for its implementation. According to the explanatory memorandum of the regulation, the flexibility of companies to choose the Corporate Governance Code they wish to apply depends on their specific characteristics, their shareholder composition and other criteria maintained in theory. However, in light of Article 17 of the Law, the Greek legal order is dominated by a code of corporate governance, the code of June 2021 issued by the Hellenic Corporate Governance Council (2021), thus creating a de facto monopoly, which doesn't seem to align with the purpose of the corporate governance provisions.

The new provision seeks to of a coherent system of corporate governance -as reflected in a code -mandatory. The concept of mandatory nature exclusively captures the adoption of a code with the characteristics of regulation and not compliance with every regulation. If a company deviates from the Code's specific provisions the principle of "compliance or justification" applies and the company needs to provide the relevant information in the Corporate Governance Statement following Article 152 of Law 4548/2018.

The Greek Corporate Governance Code is adapted to the Greek legislation and business reality and acts as a means to further enhance the value of companies, by promoting good practices and facilitating the formulation of corporate governance policies, appropriate to address the specific needs of each company.

The corporate governance framework for Greek companies with securities listed on a regulated market is twofold. On the one hand, there is the adoption of mandatory legal rules. On the other hand, there is the application of the principles of corporate governance and the adoption of best practices and recommendations via self-regulation. According to Law, the decisions of the Capital Market Commission issued under the authority of the Law embed certain provisions of Law 4548/2018 on limited companies and principles, best practices and recommendations of self-regulation, incorporated into the corporate governance code.

Other than the Code of Corporate Governance, the law obliges firms to observe an Operating Regulation. It requires that a summary be made available on the Company's website. The Company shall ensure that its significant subsidiaries also avail themselves of Operating Regulation (art. 14). The regulation of the subsidiary continues to apply to it individually and to be autonomous -so there isn't a mutual code for the whole group-, but an obligation is introduced for the parent company to procure for the adoption of it by the subsidiary. A certified auditor shall verify that the Company retains the Operating Regulation updated in compliance with the law (art. 21). The requirement to compose and comply with an Operating Regulation contributes to sound corporate governance as important aspects of it are expressly documented. This facilitates information within the company on what must be observed and respected and contributes to the development of a relevant corporate culture.

With a view to enhancing the transparency and effectiveness of the committees, referred to in Article 10 and in line with best practices in corporate governance in par. 4 of Article 10, the Law states that the remuneration committee and the nomination committee shall also have Operating Regulation, which define, inter alia, their role, the procedure for fulfilling it and the procedure for convening them. Similar obligations are laid down in Article 44(1)(b) of the Staff Regulations.

Board Committees

Remuneration and Nomination Committee

Section C of the new Law introduces two independent Board Committees. In particular, article 10 provides the obligation to establish a Remuneration Committee and Nomination Committee, whose responsibilities are defined in Articles 11 and 12 of the Law, respectively. However, par. 2 of Article 10 explicitly allows companies to delegate to a single committee the responsibilities of the remuneration committee and the nomination committee; a provision which is justified by the principle of proportionality.

Under par. 3 of Article 10, the remuneration and nomination committees must consist of at least three members. According to the same provision, all members of these committees must be non-executive, of which at least two must be independent non-executive members. The mandatory composition of these committees of only non-executive directors is dictated by the supervisory responsibilities of these committees, in areas where conflicts of interest predominantly arise.

<u>Responsibilities of the Remuneration and Nomination Committee</u>

i. The Remuneration Committee (art. 11)

(a) makes recommendations to the BoD regarding the remuneration policy (submitted for approval to the General Assembly Meeting) and the directors' and managers' remuneration, and

(b) provides the BoD with an opinion following the examination of relevant information included within the final draft of the annual remuneration report, prior to its submission to the General Meeting.

ii. The Nomination Committee (art. 12) identifies and recommends to the BoD qualified appointable candidates. Also, it is responsible for the evaluation of the body of the BoD, the individual evaluations of the CEO, the succession plan of the CEO and the Board members and the targeted composition profile of the BoD in relation to the company's strategy and suitability policy.

Audit and Risk Management Committee

<u>Audit Committee</u>

Among the Board Committees that a listed company must have is the Audit Committee, as provided for in Art. 44 of Law 4449/2017, as amended by paragraphs 4 to 7 of Art. 74 of Law 4706/2020. Based on the provisions of the aforementioned article, the Audit Committee may consist of:

a. either a committee of the Board of Directors of the audited entity, consisting of non-executive members of the Board,

b. or an independent committee, consisting of non-executive members of the Board of Directors and third parties,

c. or an independent committee, consisting only of third parties.

Also, concerning the Audit Committee, it is explicitly provided in point (g) of par. 1 of article 44 of Law 4449/2017 that its members must have sufficient knowledge of the sector in which the company operates and at least one independent non-executive member must have sufficient knowledge and experience in auditing or accounting.

The members of the audit committee are appointed by the board, where it is a committee of the board, or by the general Assembly of the audited entity or by an equivalent body, where it is an independent committee.

As regards external audit, the Audit Committee is responsible for the selection process of statutory auditors or audit firms and proposes the statutory auditors or audit firms to be appointed in accordance with Article 16 of Regulation (EU) No. 537/2014. It reviews and monitors the independence of statutory auditors or audit firms and the independence

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of statutory auditors or audit firms. It also informs the Board of Directors of the audited entity about the outcome of the statutory audit, explains how the statutory audit contributed to the integrity of the financial reporting and monitors the statutory audit of the annual and consolidated financial statements and in particular its performance, taking into account any findings of the competent authority.

Concerning the financial reporting process, the Audit Committee shall monitor the financial reporting process and make recommendations or proposals to ensure its integrity. Finally, regarding its internal control, the Audit Committee shall monitor the effectiveness of the internal control, quality assurance and risk management systems of the entity and, where applicable, of its Internal Audit Unit, in relation to the financial reporting of the audited entity.

The Audit Committee regularly informs the Board of Directors about its activities and it should submit an Annual Report to the Annual General Assembly of the company.

Risk Management Committee

In addition to the aforementioned committees, namely the audit committee, the remuneration committee and the nomination committee (the obligation to establish is laid down by law), public limited companies may choose to establish other committees if they so wish. Indicatively, there may be a strategic planning committee, a sustainable development committee or an environment, social, governance (ESG) committee, a risk management committee, an ethics committee, etc.

The Risk Committee ensures that the risk management strategy and risk appetite have been determined in accordance with the company's business plan and the company's sustainable development plan and that the company's risk management framework is appropriate and integrated into the company's decision-making process. In addition, it defines the principles of risk management. It must be stated that its establishment has been made mandatory specifically for credit institutions by Directive 2013/36/EU.

The risk committee has, in principle, distinct responsibilities from the audit committee which, inter alia, has statutory responsibility for monitoring the effectiveness of "the internal control systems for quality assurance and risk management of the entity and, where applicable, its internal audit department, in relation to the financial reporting of the audited entity ...". Under this provision, the audit committee shall monitor the effectiveness of the risk management systems not in general but in relation to the financial reporting of the company.

Before we proceed with the findings of the issue herein, it must be expressly stated that corporate governance provisions and practices stem from a wide spectrum of legislative texts and non-binding texts (i.e. Athex Group, 2019, Athex Group 2022), thus creating a multi-dimensional framework. Firms should be very aware of which provisions are legally binding and which of them entail recommendations of corporate governance best practices.

Main findings

ATHEX ESG INDEX

On June 21, 2021, the Athens Stock Exchange (ATHEX) announced the creation of its new index (ATHEX ESG Index), designed to include a maximum of 60 companies in the ATHEX Organized Market. This Index monitors the stock market performance of companies that adopt and promote their practices in issues of environment, society and corporate governance (ESG) and it is designed to help investors make informed decisions by considering companies' sustainability and ethical practices.

The first composition of the index is determined based on the ESG score resulting from the published data of 2019. Thirty-five companies participated in the initial composition of the index. The composition of the index has been revised every year. The first revision took place in November 2021 (14 additions), drawing upon the data that the listed companies published in the context of the non-financial information published in the financial year of 2020. Subsequently, the index was revised in November 2022, adding 14 companies to the ESG index; reaching the maximum number of securities set by Athens Stock Exchange for the ESG index (Athex Group, 2023). Notably, there were 3 company deletions from the ATHEX ESG Index since its establishment (Attica Bank on 31/12/2021, Europaiki Pisti on 05/08/2022 – the company delisted from Athens Stock Exchange on 03/10/2022, Plaisio Computers on 02/01/2023 – the company delisted from Athens Stock Exchange on 12/05/2023).

Sample Selection

In this study, our research focuses on the listed companies included in the ATHEX ESG Index in December 2021 (49 companies). Wherever relevant, we make comparisons with the entire population of ATHEX (147 listed companies in December 2021).

We extracted data from annual financial reports, newsletters, announcements of the Athens Stock Exchange and information notes.

Regarding our analysis for Audit and Risk committees, we have identified only 10 companies of the ATHEX ESG Index that have established a board risk committee (five of them operating in the banking sector).

Audit Committee (ATHEX)

Concerning the Audit Committee, 91% of the companies listed on the Athens Stock Exchange have a three-member audit committee, while the remaining companies have established a larger size (Graph 1).

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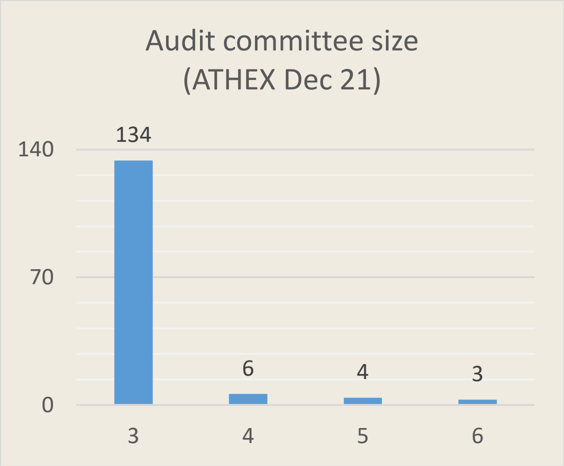
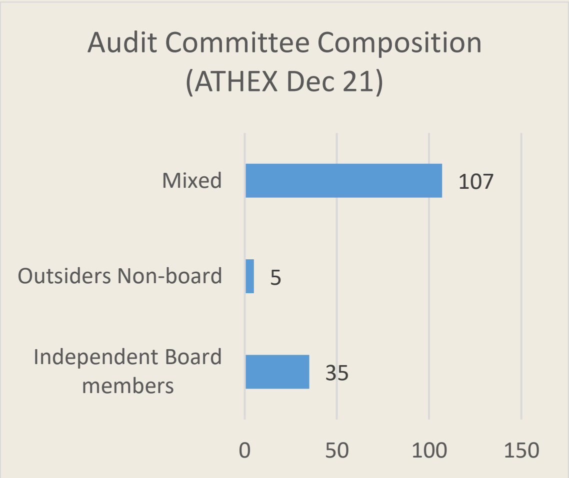


Graph 1: No of members in Audit committees (ATHEX)

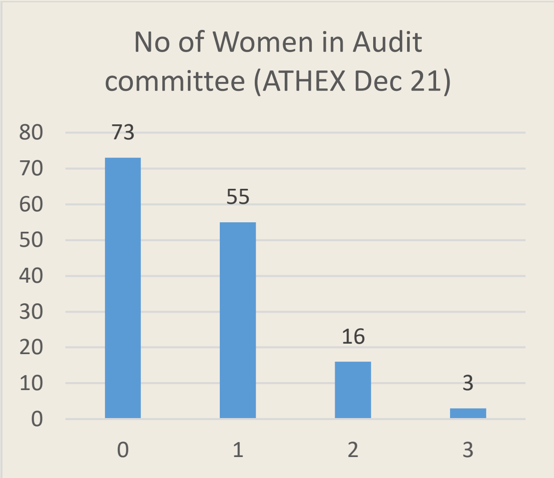
Notably, the composition of the audit committee consists of both members of the BoD and external (non-Board) members (Graph 2).



Graph 2: Audit Committee Composition

More particularly, 5 Audit Committees had committee members who were not board directors (Elinoil, General Commercial & Industrial S.A., Varvaressos, Intertech S.A., Interlife General Insurance CO), 35 committees formed exclusively with independent non-executive members and 107 committees consisting of both board and non-board members.

Regarding gender participation in audit committees (Graph 3), we observe that 50% of them (73 companies) were formed exclusively by men, whereas 1 woman included in 38% of the committees (55 companies), 2 women sat in 10% of the committees (16 companies) and finally 3 women served in 2% of the committees (3 companies).



Graph 3: Women Participation in Audit Committees

Interestingly, there were 2 audit committees that formed exclusively with women (Entersoft S.A., Kiriacoulis Mediterranean Cruises Shipping S.A.).

As for the role of the Audit Committee Chair, it has been observed that only 17% of the committees (25 companies) have assigned the Chairing duties to a woman board member.

Risk Committee (ATHEX ESG Index)

The analysis refers only to 10 companies listed in the ATHEX ESG Index that a risk committee has been established. The graphs below (Graph 4 and 5) indicate that the composition of the risk committee aligns closely with the mandates of the Corporate Governance Code.

Most risk committees consist of 3 to 5 members (average committee size is 4.4 members - see Graph 4). Considering the aforementioned 10 companies with a board risk committee, we established that:

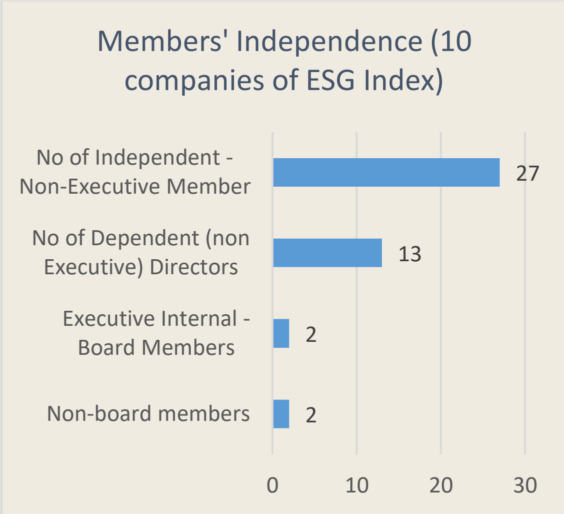
- 3 companies have a 3-member committee,
- 2 companies have a 4-member committee,
- 3 companies have a 5-member committee,
- 2 companies have a 6-member committee.

Graph 4: Risk Management Committee structure

In those 10 companies, there were 44 Board Committee positions. Out of these, females occupy only 13 of these positions (29.5%), while males occupy the remaining 31 positions (70.5%).

It is noteworthy, that there was only on woman chairing a risk committee.

Regarding the independence of the members, we found that the vast majority (61% or 27) were independent non-executive directors, (29% or 13) are dependent non-executives, and the rest are either executive members (4.5% or 2) or non-board members (4.5% or 2 – both of them found in Interlife) (Graph 5).



Graph 5: Risk Management Committee Members' Independence

To conclude, from the observations on the synthesis of the risk committees, we can infer that:

- Only 10 companies of ATHEX ESG Index have established a board risk committee, of which half companies operate in the banking sector.
- The average Risk Committee size is 4.4 members.
- Females hold 29.5% of total positions.
- Only 1 of those 10 committees was chaired by females.

Furthermore, there is a considerable overlapping between the membership of the audit and risk committees in this sample, which we believe is critical for the function of the board committees.

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Summary

From the research carried out by the Hellenic Observatory Corporate Governance for ATHEX ESG Index in December 2021, it could be derived that most of the companies in the ESG Index follow the principles of the Greek Corporate Governance Code.

The Corporate Governance Code promotes the importance of female presence on the BoD and the constituent committees. More specifically our sample (10 companies of the ATHEX ESG Index), it was found that 13 females are serving 8 Audit Committees and 11 females are serving 7 Risk Committees.

Regarding the chair of the two committees, it was observed that 4 females are chairing Audit Committees and only 1 female was chairing a Risk Committee.

Finally, from the perspective of non-Board members serving in these committees, three (3) non-Board members serve in 1 Audit Committee (Interlife) and two (2) Non-Board Members serve in 1 Risk Committee (Interlife).

Taking everything into account, we can assume that firms of the ATHEX and especially companies listed in the ESG Index should take advantage of the tools provided by the corporate governance framework (Law 4706/2020, Law 4548/2018, Corporate Governance Code, Operating Regulation, Rules of Procedure etc.), while of course complying with the legislation regarding Corporate Governance. That's the only way in which they can realise their full potential.

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