

RECOMMENDATIONS

INTRODUCTION

The closing recommendations of this report are mainly addressed at listed companies. This follows from its underlying logic and, due to previously mentioned reasons; this also led to a listing of corporate governance practices focusing mainly on the major Portuguese listed companies.

Naturally it is not the purpose of this limitation to prevent non-listed companies from extracting some benefit from some of the suggestions made here, given some necessary adaptations to these companies' circumstances. It is widely recognized nowadays that the improvement of corporate governance mechanisms is eventually linked to the general goals of optimizing corporate performance and protecting the interests of all the participants in corporate life, either as investors, creditors or employees.

It is also important to stress that these recommendations were aimed at addressing the main topics of corporate governance. This means that, based on the analysis of the international developments and discussions on these matters and on the conclusions on the practices of Portuguese companies, we tried to encompass in a systematic and coherent way the most critical aspects of the Board of Directors (structure, size, functions, directors' statute, specialised committees), the General Meeting, external and internal audits, the shareholders (including the discipline of intra-corporate business), institutional investors and the corporate conduct culture.

We recognize that ultimately this method turns these recommendations almost into a good governance code, although it was not our intention to produce a document that might conflict with other initiatives of the same nature. As mentioned before, and as has been the case in other European countries, our purpose was to make a valid contribution, in a number of detailed aspects, to a subject that matters to all the participants in the capital market.

We must remind that the publication of a set of good governance principles, such as the one contained in this document, cannot and should not be seen as a recipe that can be always enforced. The companies to which it is intended must try and extract from among these principles the rules accepted by its shareholders and considerable (considered?) applicable to its nature, size and specific characteristics.

On the other hand, it is important that all market participants are in a position so as to accurately interpret the fact that companies may comply with these principles only in a partial or limited way and not associate it automatically with a bad performance.

It is from the interaction between these two purposes that the practice and the advantages of the so-called *comply or explain* principle, already mentioned, emerge, having been adopted by a growing number of good practice codes so as to provide the market with the elements necessary to a correct judgement. The insight of that principle warrants a legitimate freedom of government options to each company, that the market may legitimate or not.

Thus, it will be possible to gain maximum utility from a set of recommendations - by confirming that they are complied with or not complied with - without compromising the underlying philosophy.

Another aspect to be mentioned is the fact that one of the consequences from the systematization followed for the model that has been adopted is that some of the recommendations inevitably encompass principles and rules already provided for - although in a different context or framework - by the legislative, regulatory and recommendatory setting in force. Accordingly the normative provisions in force that cover in part or in full the recommendations herein presented will be indicated alongside with the text.

A final reference to the fact that, although in some cases the materialization of these recommendations depends on the initiative of the companies or investors they envisage, in other cases it will depend on legislative interventions. Therefore, a special reference is made in the text to the recommendations falling in the latter case, namely by identifying where those interventions would be necessary in the existing normative framework.

CORPORATE GOALS

Listed companies must be managed with a view to maximising their value over the long-term; in other words their mission must be the creation of lasting wealth for their shareholders. However, in addition to the interests of the owners of the company's capital, many other fair and legitimate interests gravitate around a company. Those interests are protected by law, by specific agreements and by an attentive public opinion, and companies must therefore unequivocally promote the respect for those interests, even when there is a strong likelihood that a contrary practice will not be punished. In the absence of external restrictions compelling companies to respect those interests as a condition to maximise their value, we believe that they must nevertheless guide their actions by principles of sustainability and social responsibility. It is therefore recommended that:

- 1) *Listed companies have as their central goal the creation of wealth and its even distribution by all the shareholders;*
- 2) *Listed companies approve in their General Meeting and disclose their sustainable development policy and their insight on the social responsibility impeding on them, and annually inform their shareholders on the execution of that policy;*
- 3) *In addition to other aspects, the sustainable development company(?) states the energy and environment position of the company, clarifying the ecological impact of their activity and the principles guiding their actions;*

4) *The social responsibility statement of every company includes, among others:*

- *The company's staff recruitment, remuneration and career advancement policy;*
- *The company's staff vocational training and valorisation policy;*
- *The company's policy to guarantee its competitiveness, namely as regards the integration of new technologies in its production process;*
- *The company's tax management policy;*
- *The company's position vis-à-vis possible tax evasion practices by their employees, clients and suppliers;*
- *The company's cultural patronage policy;*
- *The company's policy for promoting research, scientific development and innovation;*
- *The company's position vis-à-vis the financing of political parties, governmental or non-governmental organizations and civil associations.*

5) *Information is provided on an annual basis, through the Report from the Board of Directors, on the company's relations with its main stakeholders.*

THE BOARD OF DIRECTORS

As mentioned earlier, the Portuguese legislation allows companies to be managed on a monist (Board of Directors) or dualist basis (Supervisory Board and Executive Board). We believe that both modalities may give rise to an efficient corporate governance and therefore do not recommend that one of models be adopted to the detriment of the other. It is possible, in both cases, to implement tools for the supervision and control of managing teams with executive responsibilities so as to ensure that the company is managed according to its purposes and to the interest of all its shareholders. However, hereinafter, the monist structure will be used as reference, since this is the current practice in Portugal. Nevertheless, without prejudice to the necessary adaptations imposed by the diversity of juridical systems, the references

made hereinafter to non-executive directors must be understood as also directed at the members of the Supervisory Board; the same applies to the references made to the Executive Board and its members; and as directed to the bodies of the dualist structure the references made to the Board of Directors.

BOARD OF DIRECTORS' MISSION

The mission of the Board of Directors is to ensure that the company's activity is developed in accordance with its goals. It is undoubtedly *incumbent on the Board of Directors: to define the company's strategy; to ensure the fulfilment of that strategy; to control and supervise the development of the company's business in their various components; to assess and manage the risks inherent in the company's activity; to give a fair treatment to all the shareholders; to guarantee the sufficiency, reliability and truthfulness of the disclosed information; to ensure that the company operates, in its different areas and divisions, in an effective, efficient and safe way; and to ensure that the compensation policies respect the principles of performance and merit.* In addition, it is also recommended that:

- 6) *The Board of Directors monitors the compliance with the applicable law and the company's by-laws, the respect for the principles of sustainable development and social responsibility assumed by the company, while ensuring the development of an ethical culture observed at all corporate levels.*

STRUCTURE AND INDEPENDENCE OF THE BOARD OF DIRECTORS

The problems addressed by corporate governance systems vary with the company's shareholding structure. As a result, there is not an ideal structure that can be universally applied to the relationship between the board of directors and the shareholders and to the relationship of the shareholders to one another. We believe, however, that the adoption of the recommendations

suggested below will improve listed companies' governance system, mainly of the larger ones:

- 7) *An Executive Board should be created and made responsible for the day-to-day management of the company. The functions of such a board and its modus operandi should be established in a Regulation and disclosed in the Annual Report²¹⁸;*
- 8) *The number of non-executive directors should exceed by far the number of members of the Executive Board²¹⁹;*
- 9) *Among the non-executive members there should be members that are independent from the executive directors, from the main shareholders and members with no materially relevant business or relations, capable of interfering with their freedom of judgement²²⁰;*
- 10) *The structure of the Board of Directors should reflect the shareholding structure. Its composition should observe the legitimate interests of major shareholders, minority shareholders with relevant positions and the remaining shareholders. The number of independent directors should ensure that their action is effective;*
- 11) *In the event that the shareholders control a number of voting rights that significantly exceeds the dividend rights they hold, the weight of independent directors should be reinforced so as to ensure a more effective and efficient protection of minority shareholders;*

²¹⁸ Capacity permitted by article 407-3 of the Corporate Code.

²¹⁹ Recommendation no. 5-A of the CMVM recommends the inclusion, in the board of directors, of "a sufficient number of non-executive directors"; the members of other corporate bodies may exercise ancillary roles, if the supervisory powers involved are equivalent and exercised in fact.

²²⁰ Recommendation no. 6 of the CMVM recommends the inclusion in the board of directors of "a sufficient number of independent members" and that when there is only one non-executive director, he/she must also be independent. Independent members of other corporate bodies may exercise ancillary roles, if the supervisory powers involved are equivalent and exercised in fact.

12) *Companies should publicly explain the structure of their Board of Directors, identifying in a clear and unequivocal way the identity and role of their independent directors²²¹, the dependence relations existing between executive directors and shareholders and the dependence relations existing between non-executive directors and shareholders²²².*

Size of the Board of Directors

The larger the number of directors, the stronger the Board's potential to supervise the executive directors, since a larger number of members may carry out that task. However, the increase in the number of members may curtail the celerity and efficacy of the decision-making process. Therefore, it is recommended that:

13) *Boards of Directors have a number of members that warrants an effective capacity to supervise, scrutinise and evaluate the activity of the executive directors and the fair treatment of all the shareholders; their number must however also ensure the efficacy of the decision-making process and allow the company to maximize its performance²²³;*

²²¹ It will be at each company's discretion to define "independence". In the available literature there are various definitions of "independent director". In general, the concept of independence is defined by the possibility of making a free and not conditioned judgement in case of conflicting interests in such matters as the approval of the company's accounts and the evaluation and remuneration of the executive directors (see, for instance, OECD principles). This means that only the directors with the profile and the conditions to decide against the interests of either of the parts involved in said conflicts, if they believe that to be fair and adequate, can be deemed as independent. Hence, only those that are capable of being independent vis-à-vis the executive directors and the shareholders, can be truly regarded as independent. Moreover, conflicting interests may occur vis-à-vis other parts involved in the company. This led to the adoption, following the Cadbury Report (1992), in many Good Practice Codes of a wide concept of independence, according to which independence is only possible when non-executive directors do not have, in addition to the remuneration received for the exercise of their functions (which must not be excessive so that it does not create dependence) and their own shareholding interests, any other business or relations with the company or in the orbit of the company that may materially interfere with the judgement underlying any decision.

²²² Recommendation partially covered by Chapter IV item 1. of the Annex to CMVM Regulation no. 7/2001 (model of the annual report on corporate governance).

²²³ Recommendation partially covered by the provisions of CMVM Recommendations nos. 5 and 5-A.

14) *The size of the Boards of Directors approaches European standards; when that is not the case, the reasons for that discrepancy must be clearly explained to shareholders and investors in general*²²⁴.

Transparency of the Board's Functioning

Boards of Directors must be free to define their *modus operandi* at their own discretion. However, full transparency is required as to that *modus operandi*. Specifically, it is desirable that the Board's Annual Report details:

15) *The functions of each member of the Board of Directors and its internal regulation;*

16) *The number of meetings held by the Board of Directors and by each one of its main commissions, indicating which members were present and the main topics discussed*²²⁵.

Competence, Dedication and Conditions for the Exercise of the Functions Assigned

All the members of the Board of Directors must be competent to exercise their functions and dedicate as much time as necessary to their adequate performance. In order to permit shareholders and investors in general to make a correct judgement on these aspects, it is recommended that the Annual Report discloses:

17) *The qualifications and main aspects of the curricula of the members of the Board of Directors*²²⁶;

²²⁴ As previously mentioned, the average number of members of the Board of Directors in continental Europe is 14 (Deutsche Bank, 2005).

²²⁵ Recommendation partially covered by the provisions of Chapter IV item 3 e) of the Annex to CMVM Regulation no. 7/2001, only as to the number of meetings of the Board of Directors.

²²⁶ Recommendation partially covered by the provisions of Chapter IV item 1 c) of the Annex to CMVM Regulation no. 7/2001.

18) *The other occupations of the members of the Board of Directors, including the roles they perform in other companies, clarifying any situations where they hold executive roles*²²⁷

PRESIDENCY OF THE BOARD OF DIRECTORS AND EXECUTIVE BOARD

In continental Europe a distinction is usually made between the role of the President of the Board of Directors (Chairman) and the role of the President of the Executive Board (CEO)²²⁸. In the USA, that separation is less common, but it does still exist. In general, the role of the Chairman of the Board of Directors is to head the Board of Directors; to coordinate the work of the non-executive directors, namely with regard to the surveillance, control and evaluation of the executive directors; to represent the company externally; to communicate with the shareholders; and to convey their most relevant opinions to the Board. The CEO is basically responsible for the coordination of the strategic plan's execution and the day-to-day management of the company. The separation of the roles becomes potentially more coherent with most recommendations contained in this document and that is why it is recommended. In the case where the same person is the president of the two bodies, it is necessary to ensure that the conditions are gathered for non-executive directors' work to be efficient and independent from the Executive Board. In some countries, the coordination of these functions is often assigned to one of the non-executive directors, whose experience and independence are recognized. Within this context, it is recommended that:

19) *The roles of President of the Board of Directors and President of the Executive Board are assigned to different people. In the cases where there is no separation between the roles of the President of the Board of Directors and President of the Executive Board, the companies must*

²²⁷ Recommendation partially covered by the provisions of Chapter IV item 1 b) of the Annex to CMVM Regulation no. 7/2001.

²²⁸ In other words, the distinction between the roles of the presidents of the two bodies of the dualist structure.

clarify in their Annual Report how the functions of the company's non-executive directors are coordinated and which means are in place to ensure that those directors have the necessary conditions to fulfil their mission in an effective and independent way.

NON-EXECUTIVE DIRECTORS

In Portugal, non-executive directors are traditionally seen (to a large extent) as advisors of the executive directors and (to a lesser degree) as decisors on matters where the power of decision has not been delegated²²⁹. In other countries, mainly in the USA, non-executive directors have other functions in addition to the surveillance and control of the executive directors, namely the definition of goals, the evaluation of the performance, the proposal of resignation or appointment of the executive directors. The role of the non-executive directors is, as seen above, a crucial element in the governance of US companies. In continental Europe, non-executive directors' responsibilities are being seen increasingly seen as close to those they traditionally have in the United States. Recognizing these facts and bearing in mind that the shareholding structure of Portuguese companies implies that not all the non-executive directors are independent from the major shareholders, it is recommended that:

- 20) *Non-executive directors, in addition to being advisors and decisors, should assume a role of monitoring, challenging and evaluating the executive directors and should make sure that the principles of social sustainability and social responsibility undertaken by the company are duly enforced;*
- 21) *Independent non-executive directors also assume the role of protectors of all the shareholders, namely by trying to avoid that the interest of minority shareholders are neglected to the benefit of the remaining shareholders' interests;*

²²⁹ Although article 407 no. 5 of the Corporate Code makes non-executive directors responsible for monitoring the activity of the CEO or of the Executive Board.

22) *Non-executive directors dedicate the necessary time and effort to corporate matters, so as to ensure an informed, efficient and competent accomplishment of their mission;*

23) *Non-executive directors meet, as a group, at least once a year to discuss their role and how they have been performing it.*

Similarly, it is crucial that the company grants non-executive directors with the conditions necessary to a competent and dedicated exercise of their functions. To that sense, it is recommended that:

24) *All the non-executive directors have the possibility of access to the resources necessary to the performance of their duties;*

25) *All the information requested by non-executive directors on the functioning of the Executive Board, including the agendas and minutes of their meetings, is conveyed to them;*

26) *A program is in place to introduce the new non-executive directors to the technical and financial aspects of the company, as well as a program of permanent update, so as to guarantee that non-executive directors are familiarised with corporate matters and have the necessary training and information to adequately carry out their mission.*

The compensation and the appointment may disturb non-executive directors' capacity to perform their role with freedom with respect to the executive board and, in the case of independent directors, towards the main shareholders. To avoid those situations, it is recommended that:

27) *Non-executive directors' compensation rewards the experience, competence, the time and effort dedicated to the company, without being excessive so as not to limit judgemental independence. Such compensation must be based on a fixed amount and presence checks. In must, in addition, reward the work performed by the various directors in specific Committees of the Board of Directors. On the other hand, such*

compensation must not contain any variable components indexed to stock prices nor to book ratios that may set their interests in line with those of the executive directors;

28) *Procedures are adopted to select independent non-executive directors, intended to choose professionals with the adequate qualifications and experience and avoiding that the selection method hinders their independence.*

EXECUTIVE DIRECTORS

Executive directors are responsible for carrying out the company's strategic policy by complying with the activity plan and the budget approved by the Board of Directors. In the performance of their duties, executive directors must be strictly guided by the aim of fulfilling the company's mission and goals, ensure that all the shareholders are awarded a fair treatment, independent from the company's shareholding structure. The adequate compensation of the executive directors is of major importance to keep their interests in line with those of the shareholders and to develop a culture of professionalism and transparency. To that sense, it is recommended that:

29) *Executive directors receive a compensation that adequately rewards the time, effort, experience and competence put at the service of the company; a compensation that takes into account the importance and value of the company and provides incentives to a performance aligned with the interests of all the shareholders²³⁰;*

30) *To ensure that their interests are aligned with those of the shareholders, a part of the compensation is variable and reflects the performance of each director in the fulfilment of the corporation's goals;*

²³⁰ CMVM Recommendation no. 8 advises, in general, that the remuneration of the members of the Board of Directors is structured in such a way as to permit the interests of board members to be in line with those of the company.

- 31) *The evaluation of the performance to calculate the variable portion of the compensation and its payment must be based on goals and measures that take into account the sustainability of the performance;*
- 32) *When a compensation package based on the exercise price of the company's shares is adopted, then that price cannot be revised downwards under any circumstances.*
- 33) *All the payments made to directors are reflected, at market price, as costs in the company's profit and loss account (income statement?). The annual report should contain a detailed explanation of the method used for valuating non-monetary compensations and clear information on the liabilities incurred with the pension regime.*

Like the other directors, executive directors must be aware that they have a role that is based on trust and must be renewed every year. In order to avoid the frustration of expectations, from which conflict situations may arise, and to ensure an actual freedom to dismiss a director, it is recommended that:

- 34) *Simultaneously to the determination of the executives' compensation, a severance pay to be awarded to each executive director in case of dismissal without just cause before the end of the mandate is also established.*

Executive directors must keep themselves updated and competitive not only on matters of their speciality but also on the other matters of interest to the company and on matters deriving from the company's presence in the capital market. To that purpose, it is recommended that:

- 35) *Executive directors keep permanently updated on matters of their speciality and on matters related with corporate governance and with the presence of the company in the capital market.*

SPECIALISED BOARD COMMITTEES

In addition to the Executive Board, it is useful that other specific committees are created within Boards of Directors. Henceforth we list a number of committees whose existence is recommended, except for two of them, considered not advisable (frase?). As regards the recommended committees, it is not imperative that their number and designation be as referred in this document; rather, it is important that the roles assigned to those committees are performed in the recommended terms. The only case where, due to the nature of its functions, it is believed to be of advantage to create an autonomous committee with a specific designation is the Auditing Committee. Even so, whatever committees are established, it is recommended that:

36) *The committees have specific purposes and are formalized, and their responsibilities, makeup, functioning rules and main activities developed are disclosed*²³¹

37) *The Committees give a detailed report to the Board of Directors of all the activities developed and the results obtained.*

Strategy Committee

The need may be felt for a Strategy Committee, through which a small group of members of the Board of Directors is assigned the responsibility to conceive, discuss, plan and structure the company's strategic policy, in the case where the number of board members is too large. Although this measure may render the conception and discussion of the company's strategy more effective, it causes a lesser involvement and participation of some board members in the definition of that strategic policy. It is therefore desirable that:

38) *The company's strategy is conceived, discussed, planned and structured by all the members of the Board of Directors.*

Financial and Investment Committee

²³¹ Recommendation partially covered by the provisions of Chapter IV item 2 b) of the Annex to CMVM Regulation no. 7/2001.

Companies are often faced with the need to take investment and financing decisions of different size and future relevance and sometimes crucial to their survival. Some of those decisions are recurrent and must therefore be taken by the Executive Committee in the normal exercise of its functions. There are however some decisions that concern extraordinary amounts and may have a significant impact on the company's value. Recently, in some countries, the creation Financial and Investment Committees has become more common, as a means to monitor the main decisions of the Executive Board on financial and investment matters. However, as a means to promote the involvement and participation of all board members, it is recommended that:

39) *The Board of Directors does not delegate the responsibility for any decisions involving significant risks for the company and subjects to the approval by the General Meeting the acquisitions requiring ulterior capital increase operations.*

Evaluation, Appointment and Remuneration Committee

In Portugal the formal evaluation of the Board of Directors is incumbent on the General Meeting; it is not usual for executive directors to be evaluated by non-executive ones. In addition, when the remuneration of the members of the Executive Committee, as well as of the other members of the Board of Directors, is not directly established by the General Meeting, that responsibility is assigned to a committee of shareholders appointed by the General Meeting - usually known as Remuneration Committee. We believe however that this is not the most adequate source for fixing the compensation of executive directors, since these commissions often lack adequate information and training to accomplish the mission of fixing compensation rules, i.e., to make a fair judgement of the actual performance of every executive director, which often creates a situation of dependence on the Executive Board. Moreover, the legitimacy of non-executive directors to that end is not inferior to the legitimacy of the members of the Remuneration Committee, since they are all appointed by the shareholders. Therefore, it is recommended that:

- 40) *The evaluation of the annual performance of the executive directors with respect to the compliance with the functions delegated to them and the fixing of their compensation must be assigned to all the non-executive directors. It is further recommended that the preparatory work is assigned, in the terms established by a specific regulation, to an Evaluation, Appointment and Remuneration Committee, exclusively elected and made up by non-executive directors and also including independent directors²³²;*
- 41) *This evaluation should be preceded by the definition of guidelines on its fundamental criteria in the company's by-laws or as approved by the General Meeting. The General Meeting should also establish, for each mandate, the maximum global fixed remuneration amount and the maximum percentage of profits that can be assigned to the Board of Directors' variable remuneration and pension regime;*
- 42) *The annual evaluation of the performance of the executive directors by non-executive directors should be reported to the shareholders;*
- 43) *This Committee proposes the Board and the Board proposes the General Meeting the prior approval of all compensation plans based on the assignment of shares and/or stock options applicable either to the members of the Executive Board or to officers and employees other than directors²³³;*
- 44) *The definition of the compensation policy for the company's senior staff, as well as the fixing of rules for the evaluation of their performance is assigned to the Board of Directors that should try to create - on the basis*

²³² As article 399 of the Corporate Code assigns the General Meeting of Shareholders, or a commission created by that body, the responsibility for fixing the remuneration of each director, the application of this recommendation will require that the law be amended accordingly.

²³³ Recommendation covered by CMVM Recommendation no. 10, as regards the approval by the General Meeting of the plans for the assignment of shares and/or stock options to directors or employees.

of a proposal submitted by the Evaluation, Appointment and Remuneration Committee - a transparent, balance and competitive plan and not become a constraint to the determination of the executives' compensation;

45) *The Board of Directors informs the shareholders on an annual basis, within the scope of the Annual Report, on the makeup and activity of this Committee, namely on the methodology and criteria used in the evaluations;*

46) *The Annual Report contains information on the compensation of each member of the Board of Directors, with the distinction, in the case of the members of the Executive Board, between the fixed and variable component. In our opinion, the minimum information on these matters includes the compensation of the President of the Board of Directors, the fixed and variable compensation of the President of the Executive Board, the fixed and variable compensation of the Vice-President of the Executive Board, the fixed and variable compensation of the remaining members of the Executive Board and an indication as to the range of the individual compensation of the other members of the Executive Board. As regards non-executive directors, the minimum information is the compensation of the members to which the compensation is granted and the range of the individual compensation. Information should also be disclosed on the compensation received in other companies of the same group or in representation of the group towards third parties, regardless of the roles performed. Furthermore, information should be disclosed on the compensation received by the executive directors regarding functions directly or indirectly carried out in companies controlled by reference shareholders²³⁴.*

²³⁴ Recommendation partially covered by the provisions of Chapter IV no. 5 of the Annex to CMVM Regulation no. 7/2001.

An aspect that is often neglected by Portuguese companies and needs to be quickly corrected is the formalisation and disclosure of appointment processes. To that sense, it is recommended that:

- 47) *In the event that it is necessary to co-opt a director, the selection process is conducted by the Evaluation, Appointment and Remuneration Committee, which must submit the Board of Directors a duly founded proposal.*
- 48) *The co-optation of new directors is explained and justified in the Annual Report addressed to the shareholders;*
- 49) *Any proposal submitted to the General Meeting for ratification of directors' co-optation or any other proposal of a list for a new election is founded on the work developed by this Committee;*
- 50) *The Evaluation, Appointment and Remuneration Committee monitors the selection and appointment of senior staff, so as to guarantee that the company has a basis for recruiting future executive directors that warrants a smooth process in case of future successions.*

Auditing Committee

A crucial element of any corporate governance system is the soundness, reliability and sufficiency of the economic and financial information released. That information is based on documents and reports prepared by the company's financial department, and its conformity with the applicable rules, as well as its authenticity and completeness should be audited. Without prejudice to the existence of internal auditing mechanisms, such reports should be analysed by external auditors that are independent, competent and qualified according to the strictest international standards. It is incumbent on the Board of Directors to make sure that this takes place. For the purpose, it is recommended that:

- 51) *An Auditing Committee is created within the range of the Board of Directors, exclusively elected and made up by non executive directors,*

*with a majority of independent directors, of which one has the role of president. The purpose of this committee is, in accordance with an appropriate regulation, to ensure that the financial information was actually analysed by external auditors that are independent, competent and qualified according to the strictest international standards, and that the released information reflects the actual situation of the company*²³⁵

52) *The Auditing Committee includes at least one member of recognized competence and reputation in the financial, accounting and auditing areas and one member with operating knowledge on the company's main business;*

53) *None of the members of the Auditing Committee is part of it for more than two consecutive mandates;*

54) *This Auditing Committee defines the scope and depth of external auditing services, including the approval of action plans and activity programs. It must also choose the entity that will render these services, negotiate its compensation and ensure that the conditions necessary to the rendering of such services exist in the company;*

55) *The Auditing Committee is the interlocutor of the company with the external auditor and the first recipient of its audit reports;*

56) *The rendering of non-auditing services by the external auditor is subject to prior approval by the Auditing Committee, which must refuse it in case it believes that the independence of said auditor is not guaranteed.*

57) *The Auditing Committee discloses, in the Report of the Board of Directors, all the economic relations of the company with the external auditor,*

²³⁵ Although the compliance with recommendations 53) to 65) (creation of the Auditing Committee and definition of its role) does not require any immediate law amendments, it is necessary to bear in mind that the review of the EU 8th Directive on the legal certification of accounts and its transposition to the Portuguese juridical order may lead to amendments in the existing laws, as well as in the principles and rules proposed in those recommendations. See above (Chapter II, 4.2.4. (iv) *Compliance with EC Action Plans*) the origin and main aspects of the review of the 8th Directive within the scope of the action plan "Strengthening the legal certification of accounts in the European Union."

detailing all the amounts paid and separating auditing from non-auditing services²³⁶;

- 58) The Auditing Committee evaluates every year the work carried out by the external auditor and with the same periodicity confirms the auditor or replaces him/her by another auditor, informing the General Meeting of the reasons for that replacement;*
- 59) The Auditing Committee is also responsible for the supervision of the internal control and risk control systems, without prejudice to the functional control of the Executive Board on these services;*
- 60) The competences of the Auditing Committee mentioned in the previous paragraph includes the approval of the handbooks of the internal auditing department, the approval of its plan and activity program and the knowledge on the main conclusions and recommendations of the existing auditing reports;*
- 61) The Auditing Committee promotes the articulation and comparison between internal and external auditing reports;*
- 62) The Auditing Committee promotes, encourages and facilitates the internal disclosure of information on illicit or anti-ethical practices²³⁷;*
- 63) The Auditing Committee has the power to hire third party services judged necessary to the good performance of its functions;*
- 64) The Auditing Committee keeps the Board of Directors informed on the development of its activity on a permanent basis, and the shareholders within the scope of the Annual Report of the Board of Directors.*

Corporate Governance Committee

²³⁶ Recommendation covered by the provisions of Chapter I no. 10 of the Annex to CMVM Regulation no. 7/2001.

²³⁷ Recommendation covered by CMVM Recommendation no. 10-A, as to the existence of a policy of internal communication of irregularities.

The governance of the company and the efficiency of the Board of Directors and of its various Committees must be periodically evaluated by the Board of Directors. The accomplishment of this mission in an operational way justifies its delegation to a Committee - either an autonomous committee or the Evaluation, Appointment and Remuneration Committee. Whatever the chosen framework, it is recommended that:

- 65) *The Board of Directors evaluates its global performance, as well as the performance of the various committees existing in addition to the Executive Board and the governance system adopted. The preparatory work can be assigned to a specific Committee²³⁸;*
- 66) *The annual report of the Board of Directors reports on the activity mentioned in the previous paragraph and presents the measures already implemented or to be implemented to improve the company's governance system.*

EXTERNAL AUDITING

External auditing is one of the pillars of any governance system, since the quality and reliability of the company's economic and financial information emerge from the efficacy, completeness and independence of external auditors' work. They are therefore responsible for carrying out a work of uncontroversial technical value, with the appropriate depth and extension and completely independent from the Board of Directors, any individual shareholders or any other private interests. Its sole purpose must be to ensure that the reported information gives an accurate picture of the company's economic and financial situation. To that purpose, and to guarantee an image of credibility and independence, it is recommended that:

²³⁸ CMVM Recommendation no. 7 recommends the creation of internal Auditing Committees, with the power to assess the corporate structure and its governance.

- 67) *External auditors abstain from putting themselves in a situation of dependence vis-à-vis any company or group of companies, namely they should avoid that one particular customers accounts for a significant portion of their trade volume;*
- 68) *Audit companies disclose their trade volume, a list of clients (companies and groups of companies) accounting for over 5 per cent of their total income, and report the individual percentage of each one of those clients;*
- 69) *In case the company opts for auditor rotation, in line with the options provided for by the 8th Directive, the ceasing auditor undertakes to make a loyal and accurate transition to the new auditor;*
- 70) *In case the company opts for partner rotation, in line with the options provided for by the 8th Directive, the ceasing partner undertakes to make a loyal and accurate transition to the new partner;*
- 71) *The partners or employees of the auditing company do not work not receive any compensation for future work in a company where he/she has rendered auditing services at least within two years after the termination of those services.*

INTERNAL AUDITING AND OTHER INTERNAL STRUCTURES FOR RISK DETECTION AND MANAGEMENT

Boards of Directors must set up and keep in place effective and efficient structures for risk detection and management, regarding not only the company's present activities but also new ones. For that purpose, it is recommended that:

- 72) *The Board of Directors keeps in place an adequate internal control system to protect shareholders' interests, the company's investments and assets and, in addition, reviews at least once a year the efficacy and efficiency of that system, reporting the results to the company's shareholders.*

SUPERVISORY BOARD

The opinion has been previously expressed that the responsibility of ensuring that the financial information was actually analysed by external auditors that are independent, competent and qualified according to the strictest international standards, and that the released information reflects the actual situation of the company must be assigned to an Auditing Committee created within the scope of the Board of Directors. This means that desirably the responsibilities presently assigned to the Supervisory Board regarding those matters should be transferred to that committee. That measure is justified by a number of reasons: i) Non-executive directors, as well as the members of the Supervisory Board, are elected by the General Meeting, thus being equally legitimate; ii) More information and a wider power to accede to information will be available to the members of the Auditing Committee than to the members of the Supervisory Board, due to the fact that they attend the meetings of the Board of Directors and are part of the Board; iii) The members of the Auditing Committee, once they also belong to the Board of Directors, have a stronger influence on the executive directors and on the company's technical structure than the members of the Supervisory Board; iv) It is incumbent on the members of the Auditing Committee to select, hire, dismiss and monitor the activity of external auditors, contrarily to the Supervisory Board, a mere recipient of the final report.

This matter must obviously be analysed in the light of the corporate law, so as to safeguard, if judged necessary, the goals that led to the assignment of other powers to Supervisory Boards, namely the monitoring of the company's management and the compliance with the law and the company's by-laws. It is therefore recommended that:

73) The extinction of Supervisory Boards is considered in companies with the conditions to have Auditing Committees, transferring to those Committees the responsibilities and powers to check the accuracy and reliability of the financial information and preserving the wider

provisions of the corporate law regarding other functions presently assigned to Supervisory Boards²³⁹;

74) In the companies that, due to their smaller size, do not gather the conditions to have Auditing Committees, it must be ensured that the Supervisory Board will carry out the functions assigned by this document to those Committees.

REMUNERATION COMMITTEES

The Portuguese law assigns the General Meeting or a committee of shareholders appointed by the General Meeting the responsibility of determining the compensation of all the members of the Board of Directors. It has already been mentioned that we consider it recommendable that the determination of the executives' compensation and the evaluation of their performance is entirely assigned to non-executive directors, the preparatory work being incumbent on an Evaluation, Appointment and Remuneration Committee. Concomitantly, it is recommendable that:

75) The compensation of non-executive directors is determined directly by the General Meeting or by a committee of shareholders appointed by the General Meeting.

GENERAL MEETINGS

As previously mentioned, in Portugal, according to most opinions gathered, general meetings do no longer control corporate managers. With the perspective of increasing the efficiency and efficacy of this body, it is recommended that:

²³⁹ The extinction of Supervisory Boards in the terms proposed by Recommendation 73) and the review of their functions in the terms proposed by Recommendation 74) will require the introduction of amendments to the laws regulating the existence and framework of Supervisory Boards.

- 76) *The President of the General Meeting is independent both from the Executive Board and the company's main shareholders, and acts as such;*
- 77) *All the shareholders have an active role, assuming their quality of owners of the company;*
- 78) *New technologies are adopted to communicate with the shareholders and in their participation in the General Meeting, so that the shareholders may be effectively and timely informed on the matters that will be discussed and may participate in the discussion²⁴⁰. It is also recommended that the company's website displays on a permanent basis all the Annual Reports and all the other information allowing existing and potential investors to trace the company's economic and financial history;*
- 79) *More specifically, any shareholder is allowed to submit, disclose and justify proposals to be voted in the General Meeting through the company's website or through the e-mail tools used by the company to communicate with its shareholders and with investors in general.*

MEASURES CONTRARY TO THE FUNCTIONING OF THE MARKET FOR CORPORATE CONTROL

It is acknowledged that the market for corporate control is governed by other reasons beyond the mere penalization of inadequate performance by managements' teams. However, in order to improve the efficiency of corporate governance, it is recommended that:

- 80) *Any measures that may hinder the functioning of the market for corporate control are abolished;*
- 81) *The one share one vote principle is encouraged and the percentage of voting rights coincides with each shareholder's cash flow rights.*

BUSINESS WITH SHAREHOLDERS AND IMPORTANT TRADE RELATIONS

²⁴⁰ Recommendation covered by article 3-A of CMVM Regulation no. 11/2003.

The existence of business relations with majority shareholders or influential minority shareholders may damage small shareholders. Therefore, it is recommended that:

82) *Shareholders with holdings exceeding five per cent of the company's share capital identify to the Board of Directors all the company's suppliers and clients with each they have common relevant business interests;*

83) *All the transactions of the company with shareholders with holdings above two per cent or with third parties with which they have common relevant business interests are carried out according to market conditions; when those transactions are not effected under market conditions, it is recommended that they are previously approved by the Board of Directors or by the Auditing Committee, as defined in either regulation;*

84) *The transactions of the company with shareholders with holdings above two per cent or with third parties with which they have common relevant business interests are communicated to the remaining shareholders on an annual basis, together with the indication as to the procedures adopted in the negotiation of those transactions;*

85) *The Board of Directors discloses and characterises all the important relations in obtaining financing operations and in rendering relevant services, with a clear indication of the institutions approached for funding, advisory and consultancy purposes and the relative weight of each of these services. (frase?)*

TRANSACTIONS ON OWN SHARES

Without prejudice to other practices intended to keep market integrity determined by law or by each company's conduct code, it is recommendable that:

86) *The shareholders with relevant holdings in the company, the directors and senior officers with access to privileged information about the company provide the Board of Directors with exhaustive and detailed information about the transactions they made on securities belonging to the company or to affiliated companies. The company's directors and senior officers must abstain from transacting securities issued by the companies within the periods established for disclosure of relevant information; (frase?)*

87) *The profits obtained with the acquisition or sale of shares making use of privileged information are not appropriated by those buyers or sellers²⁴¹.*

CONFIDENTIAL EXPENSES

Confidential expenses are opaque and may be conflicting with the interests of the shareholders and/or with the company as a whole and damage investors' confidence. Therefore, it is recommended that:

88) *The practice of accounting for confidential or non documented expenses is not only subject to tax aggravation but eliminated, and the law no longer permits their existence²⁴².*

DIVIDEND POLICY

Shareholders are entitled to dividends. The distribution of dividends must occur whenever the company has profits and does not have investment

²⁴¹ As mentioned in footnote no. 126, in 2005, following the legislative authorisation contained in Law 55/2005 of 18th November, the Securities Code was reviewed, with the purpose of transposing to the Portuguese juridical order Directive 2003/6/EC on "insider trading". Among the new provisions is the one that stipulates, within the spirit of this recommendation, that the asset advantages resulting from crimes of insider trading or market manipulation are apprehended and primarily assigned to the compensation of the damaged parties that have complained in the criminal proceeding.

²⁴² The prohibition to account for confidential or non documented expenses will require that the law in force be amended, as it authorizes them, although it does not accept them as tax costs and imposes on them an autonomous tax rate.

opportunities that are considered attractive enough. Within this scope, it is recommended that:

89) *The Board of Directors submits to the approval by the General Meeting a long-term dividend policy;*

90) *The Board of Directors announces and explains any alteration they intend to propose to the General Meeting regarding the dividend policy and, in particular, justifies in detail the purposes of the investment and the return prospects whenever the level of dividends to be distributed is below the level that had been foreseen, in relative or absolute terms.*

CODES OF ETHICS AND CONDUCT

As previously mentioned Boards of Directors must develop an ethical culture and implement it at all corporate levels. The existence and application of a Code of Ethics or Conduct will certainly contribute to that purpose. It is therefore recommended that:

91) *Companies have Codes of Ethics or Conduct, disseminate them and take measures to promote the compliance with those codes;*

92) *Such Codes determine that directors, senior officers and other employees with access to privileged information must abstain from making transactions in periods where material events will be disclosed, namely the announcement of the company's results, and also abstain from making very short-term transactions in the terms defined in those codes.*

INSTITUTIONAL INVESTORS

Due to their size and sophistication, institutional investors play a special role in capital markets. They have therefore an accrued obligation to contribute to the smooth functioning and reliability of those markets. In that sense, it is recommended that:

- 93) *Institutional investors lay out the main guidelines of the corporate governance policy they deem to be the most appropriate, identifying the practices they recommend and those they consider contrary to the interests of corporate shareholders, and strive to adopt measures ensuring that those guidelines are complied with;*
- 94) *Institutional investors act as true shareholders, exclusively in the interest of their participants, namely by taking an active role in the companies' general meetings, publicly justifying how they exercised their voting rights and explaining the coherence of that exercise with the policy they adopt in matters of corporate governance²⁴³;*
- 95) *Institutional investors contribute, by exercising their voting rights, to the implementation of good governance practices in the companies.*

THE STATE AS SHAREHOLDER

The Portuguese state keeps relevant holdings in the capital of some listed companies. The state has the duty to exercise its property and control rights. The exercise of the State's shareholding powers cannot however be mingled with the exercise of its power to regulate and define policies for the different industries. To that sense, it is recommended that:

- 96) The State exercises its rights as shareholder of listed companies as if it were a private shareholder and abstains from using those companies as instruments of regulation or industrial policy.

²⁴³ According to the Legal Framework for Collective Investment Undertakings (Decree-Law no. 252/2003 of 17th October) and to CMVM Regulation no. 15/2003, the managing entities of undertaking for collective investment in securities must report to the CMVM and to the market the justification for exercising the right to vote inherent to the shares in the portfolios they manage; that communication is obligatory when those rights exceed two per cent of the voting rights corresponding to the capital of the issuing company.