



BUDAPEST STOCK EXCHANGE LTD.

**CORPORATE GOVERNANCE COMMITTEE
MONITORING REPORT**

**ON COMPLIANCE WITH THE CORPORATE
GOVERNANCE RECOMMENDATIONS**



November 2016



Table of Contents

I. INTRODUCTION	3
II. REPORT.....	4
III. COMPLIANCE WITH THE CORPORATE GOVERNANCE RECOMMENDATIONS	5
1.1 General Principles: Provision of Information, Voting Rights.....	5
1.2–1.3 General Meeting	5
2.1–2.3 Meetings of the Administrative Board, Board of Directors, Supervisory Committee.....	6
2.5–2.6 Transparency, flow of information, conflicts of interest, and independence in the Administrative Board, Board of Directors, and the supervisory committee	8
2.7 Performance evaluation, remuneration of the Board of Directors/administrative board, supervisory committee	9
2.8 The System of Internal Controls and Risk Management.....	11
2.9 External Advisor, Auditor.....	12
3.1 Committees: General Principles	13
3.2 Audit Committee	13
3.3 Nominating Committee.....	14
3.4 Remuneration Committee	14
3.5 Merging Committees	15
4. Transparency and Disclosure.....	15
IV. CONCLUSIONS	18
1. Summary Conclusions	18
2. Other general conclusions.....	19

I. INTRODUCTION

The general purpose of the application of corporate governance recommendations is to promote the transparent and efficient operation of the market, to support the implementation and enforcement of legislation, especially in terms of shareholders' rights and ownership functions, and to harmonise the interests of the issuers, the investors and the issuing company's environment. Effective corporate governance facilitates growth in the issuing company's value, and also ensures that the rights of shareholders and other stakeholders are well-represented.

The Budapest Stock Exchange (BSE) published its Responsible Corporate Governance Recommendations in 2004, which was later superseded by the Corporate Governance Recommendations. The Corporate Governance Recommendations were last amended in 2012. In addition to the amendment of the Recommendations the external – community and domestic – legal environment has also changed: Act V of 2013 on the Civil Code (Civil Code) entered into force on 15 March 2014, and issuers have gradually rolled out the new provisions of the Civil Code.

According to Commission Recommendation 2014/208/EU¹, in order to motivate companies to comply with the relevant corporate governance code or to better explain departures from it, efficient monitoring needs to be carried out at the national level, within the framework of the existing monitoring arrangements.

As a professional committee of the BSE, the general tasks of the Corporate Governance Committee (Committee) include the supervision of the continued development of Corporate Governance Recommendations by taking domestic industry requirements, EU legislation under drafting and general international trends into consideration, and the representation of industry considerations in the field of the further development of corporate law. In compliance with the provisions of Commission Recommendation 2014/208/EU, this is the first year when the Committee, in cooperation with Forrai Law Offices, will provide, by way of this Monitoring Report, a summary of the level of compliance of issuers' corporate governance reports with the recommendations and proposals of the BSE.

Based on the unique methodology applied for the purposes of this Monitoring Report, the Report focuses on the statistical data included in the corporate governance reports that concern levels of compliance, emphasising the reasons underlying more important deviations, or deviations that can be generalised (in certain cases per issuer category). For this reason, the aggregations are based on the complete acceptance of the corporate governance reports from the issuers, with the caveat that, in some cases, we had to point out conflicts in the data and, in certain cases, the lack of coherence.

The Committee hopes that it will be able to present those interested and the public with the trends of compliance with its recommendations, as well as compare compliance ratios against previous years' data in its future Monitoring Reports.

¹ Commission Recommendation of 9 April 2014 on the quality of corporate governance reporting ('comply or explain') (2014/208/EU),

II. REPORT

Annex 1 to the Corporate Governance Recommendations of the BSE requires that issuers report on their corporate governance practices in their corporate governance reports in a transparent and clear manner, and elaborate if their practice deviates from the recommendations formulated in the Corporate Governance Recommendations and provide explanations for such deviations. The Corporate Governance Recommendations contain aspects to be taken into account when drawing up these reports, and the availability and main content-related deficiencies of these aspects was reviewed by the Committee as part of its monitoring activity.

Overall, it can be established that many issuers – primarily listed in standard and technical categories – did not prepare reports at all, or their reports were highly incomplete. In general, it can also be stated that in the case of certain issuers, the report as specified in Annex 1 to the Corporate Governance Recommendations is not adequately detailed and does not comprehensively cover the aspects recommended by the BSE, and that the typical shortcomings relating to the various aspects have also been identified:

- The brief presentation of the operation of the administrative board/Board of Directors, and the sharing of responsibilities and tasks between the administrative board/Board of Directors and management was missing from the reports of six issuers (13.9%), and was incompletely presented in the case of nine other issuers (in these cases, typically the presentation of the sharing of responsibilities and tasks between the administrative board/Board of Directors and management was missing).
- The presentation of the members of the administrative board/Board of Directors, supervisory committee and management was missing from the reports of nine issuers (20.9%), and was incomplete in a few other cases (in these cases, typically the indication pertaining to independence, and the presentation of professional careers and management were missing from the report).
- Specifying the number of meetings of the administrative board/Board of Directors, supervisory committee or committees held in the given period was missing from the reports of approximately one quarter (25.5%) of issuers, and was incomplete in a few other cases (in these cases, typically the specification of participation ratios was missing from the report).
- During the evaluation of the work of the administrative board/Board of Directors, supervisory committee and management and of the various members was missing from the reports of 28 issuers (65.1% – primarily listed in standard and technical categories), and was incomplete in terms of content in a few other cases (in these cases, typically the aspects of evaluation were missing from the report).
- In many cases, the report on the operation of the various committees was incomplete: 15 issuers (34.8% – primarily listed in standard and technical categories) did not elaborate on this aspect at all, while 20 other issuers (46.5%) elaborated incompletely (see Sections III. 3.1-5 below). Typically, the professional presentation of committee members and presentation of the key topics discussed were missing.
- More than half of the issuers (primarily listed in standard and technical categories), or 25 companies (58.1%) failed to present their system of internal controls, the assessment of activity in the given period or their report on the efficiency and effectiveness of risk management processes. In addition, four other issuers (9.3%) failed to comprehensively

elaborate on this aspect (typically the report on the efficiency and effectiveness of risk management processes was missing).

- Ten issuers (23.2%) failed to provide information on whether the auditor performed any activities not related to auditing.
- The in-depth presentation of the company's disclosure policy and the policy pertaining to insider trading was missing for 11 issuers (25.5%).
- The in-depth presentation of the method of exercising shareholder rights was also missing for 11 issuers (25.5%).
- Nine issuers (20.9%) failed to provide information on the rules pertaining to the conduct of the general meeting.
- Approximately half (51.1%) of issuers did not prepare a remuneration declaration as part of its corporate governance report and, in a few other cases, the remuneration declaration also did not contain comprehensive information.

III. COMPLIANCE WITH THE CORPORATE GOVERNANCE RECOMMENDATIONS

Annex no. 2 and 3 of the Corporate Governance Recommendations of the BSE require that issuers declare the extent to which they have implemented the recommendations, proposals specified in the relevant sections of the Corporate Governance Recommendations of the BSE, by completing tables as part of their corporate governance reports. The Monitoring Report below contains a summary assessment of these issuer declarations.

1.1 General Principles: Provision of Information, Voting Rights

1.1.1 All issuers complied with the BSE recommendation that specifies that the Administrative Board or the Board of Directors must ensure that shareholders have timely access to any information that is essential for their ability to exercise their rights. Although three issuers completed an older version, this did not impact the provision of information in due time. It should be noted, however, that in regards to certain related information recommendations, proposals issuers' compliance is not complete (see sections 2.5.4, 2.5.6, 2.7.1, 4.1.6, 4.1.9, below etc.).

A large majority (81%) of the issuers complied with the recommendation that the company must apply the principle of "one share one vote". Several of the issuers in the remaining 19% issued preferred stocks, which provide voting rights of different extents and weights. Furthermore, some issuers also issued non-voting preferred stock with liquidation preference and/or non-voting preferred stock with dividend preference.

1.2–1.3 General Meeting

1.2.8 100% of the companies complied with a recommendation that requires companies to ensure that shareholders are able to participate in the general meeting under the same conditions.

1.2.9 Based on the recommendation, the agenda items for the general meeting of the company are specifically identified and drafted, and no other agenda items are discussed during the meeting. All companies except one complied with this recommendation. The issuer that failed to comply with this requirement explained its departure from the recommendation by stating that in general, the nature of the matters discussed does not necessitate the Administrative Board to elaborate in its proposal on explaining the impact of decisions, although it did indicate that if deemed necessary, it does do this.

Barely more than half of BSE issuers (53.5%) ensured that the draft resolutions for the general meeting mention the recommendation of the supervisory committee, and to detail the expected impact of the decision. The majority of the issuers that did not comply with the recommendation (27.9%) did not comply with the recommendation because they do not have a supervisory committee in place, therefore, they are unable to mention the opinions of such a committee. Another 18.6% of the issuers considered that the nature of such decisions did not necessitate explaining the impact of the decisions in detail in the proposals, and there are also issuers who provide such explanations in response to questions asked at the general meeting. Furthermore, there are companies that publish the draft resolution separately.

1.2.10 Slightly more than half (53.5%) of the issuers published shareholders' comments on the agenda items of the general meeting two days prior to the general meeting. The reason why the remaining issuers (46.5%) did not comply with the mentioned recommendation is that shareholders did not modify or provide comments on the agenda items, so the question of compliance with the recommendation did not apply. (There were issuers that mentioned that even though they have not been compliant with the recommendation due to the above reason, as soon as such modifications or comments are received, they will publish them two days prior to the date of the general meeting.)

1.3.8 The BSE also formulated a recommendation that shareholders should be made aware of the observations made regarding the agenda items of the general meeting concurrently with registration at the latest, and that written observations received regarding agenda items be published two business days prior to the general meeting. The compliance rate is identical to those specified above, as 53.5% of issuers complied with the recommendation, while the remaining 46.5% failed to comply only because they did not make observations regarding agenda items.

1.3.10 Based on the recommendation of the BSE, the election and recall of executive officers should be provided for in separate resolutions for each person, instead of including several persons in one resolution. The level of compliance with this recommendation was also high, as 93% of issuers adhered to the above requirement. Among the remaining 7% of issuers, many failed to comply as no executive officer was elected or recalled, while one issuer departed from the recommendation due to simplification. It should be noted with regard to these results that the interpretations applied by the issuers are not uniform as they avail themselves of the opportunity – available since the amendment of the Corporate Governance Recommendations in 2012 – to provide an answer of “Yes” to questions that are event-based if no such event occurred during the business year in question, but based on the statutes of the company and/or its practice, the company would have acted in accordance with the Corporate Governance Recommendations, had such an event occurred.

2.1–2.3 Meetings of the Administrative Board, Board of Directors, Supervisory Committee

2.1.1 The BSE drafted a recommendation on which areas it considers to be the most important tasks of the Administrative Board/Board of Directors. The specific tasks noted were the following: participation in the determination of strategic policies; verification of the execution of financial steps;

together with the supervisory committee, identification and supervision of corporate objectives; ensuring the integrity financial and accounting reports; definition of remuneration and award principles; management of conflicts of interest; determination of risk management policies; development of appointment and leadership succession mechanisms; drafting and supervision of transparency policies; supervision of the effectiveness and efficiency of the corporate governance practice; and the development of the appropriate method of relationship management. The vast majority of companies (95.3%) complied with the recommendation, while among the remaining 4.7% of those that failed to comply, one cited the fact that although the tasks fall under the competence of the Administrative Board, in line with the regulations set out by the company, the tasks of the Administrative Board do not fully cover the list. The other – non-compliant – issuer stated that the nature of the company's activities makes the use of different solutions necessary.

2.3.1 According to the proposal of the BSE, the Administrative Board/Board of Directors should conduct meetings at regular, precisely identified frequencies. The vast majority of the issuers (86%) complied with this recommendation. Different reasons were stated by the other 14% of issuers, explaining their departure from the recommendation. Therefore, in the cases of most of the non-compliant issuers, meetings were convened as/if necessary, but there was one company where the daily communication of Administrative Board members justified departure from the recommendation. It should be noted that, according to the Civil Code, the administrative board/Board of Directors should prepare a report on the executive management, the asset situation of the company and its business policy for the general meeting at least once in a year, and if the corporation has a supervisory committee, a report on the same should be prepared for the supervisory committee every three months.² As a result, departure from the recommendation could also mean non-compliance.

The recommendation of holding meetings at a regular, pre-identified frequency has also been raised as it pertains to the supervisory committee. The majority of issuers (72.1%) complied with the recommendation, while the issuers that did not comply with the recommendation (27.9%), were not able to do so due to the lack of a supervisory committee.

The BSE issued a recommendation on ensuring that the administrative board/Board of Directors provide for the conduct of meetings that cannot be planned in advance, and on the matter of providing for decision-making via electronic means in the interest of ensuring that the meeting can be conducted without hindrance. 93% of issuers complied with the above recommendation, while for 7% of issuers, one of the reasons was the lack of provisions on the use of electronic telecommunication means or, in another case, the holding of extraordinary meetings with the requirement of in-person attendance.

The BSE also issued the above recommendation with respect to supervisory committees, meaning that the rules of procedure supervisory committees should also provide for the conduct of meetings that cannot be planned in advance, as well as on decision-making via electronic means. The majority of the issuers (65.1%) complied with the above recommendation, with 23.2% of the non-compliant issuers stating that the reason underlying the non-compliance is that no supervisory committee exists in the companies, whereas in 11.7% of cases departures stemmed from the prohibition of extraordinary meetings, holding of extraordinary meetings with the requirement of in person attendance, or lack of provisions on the use of electronic telecommunication means, and in one case no explanation was provided.

² Section 3:284 (1) of Act IV of 2013 on the Civil Code.

2.5–2.6 Transparency, flow of information, conflicts of interest, and independence in the Administrative Board, Board of Directors, and the supervisory committee

2.5.1 A large majority, 90.7% of the issuers, complied with the recommendation that in the interest of ensuring impartiality, there should be a sufficient number of independent members in the Administrative Board, Board of Directors, and supervisory committee. Among the remaining 9.3% of issuers, one company did not provide an explanation. The explanations from another three non-compliant issuers was not sufficient, as they did not provide a specific explanation for their lack of compliance with the recommendation. (Therefore, the explanations that stated that “persons delegated by the company’s shareholders are part of the Administrative Board” or that “the majority of the members of the supervisory committee must satisfy the relevant independence criteria in a company that has a Board of Directors that operates a non-uniform governance system” are not sufficient. Neither is the explanation according to which “the Administrative Board coordinates the operation of the company adequately, and only the supervisory committee has independent members).

2.5.4 The BSE made a recommendation according to which the administrative board/Board of Directors should require its members to confirm their independence on a regular basis (in connection with the annual FT report). The relative majority (69.7%) of issuers complied with the recommendation. 4.6% of the issuers partially complied with the recommendation, while the others did not comply with the recommendation, as one of them stated that the company did not have a supervisory committee in the year in question, whereas in the case of another, the Administrative Board did not comply with the requirement, but the supervisory committees did. Of the 25.7% non-compliant issuers, three stated that the Civil Code does not require companies to confirm the independence of the executive body members, and used this argument to explain the departure from the recommendation. Two issuers did not provide an explanation. In another, members provide updates on any changes in their status proactively to issuers. In their explanations, the other issuers stated that independent members satisfy the relevant criteria.

2.5.6 Based on the recommendation of the BSE, companies are advised to publish on their websites the independence criteria applied to their Administrative Board, Board of Directors, and supervisory committee. Only 26.2% of issuers complied with the recommendation. Among the large majority, 73.8% of issuers, not complying with the recommendation, most companies cited the fact that they acted pursuant to the provisions of the Civil Code; there were some companies that referred to the absence of a supervisory committee; while many others mentioned that the rules of procedure contain the criteria of conflict-of-interest and independence, rules which are published on their websites.

2.6.1 Based on the recommendation of the BSE, the member of the Administrative Board/Board of Directors informs the body and the supervisory committee or the audit committee if they personally have a significant interest in one of the transactions of the company or any of the subsidiaries thereof, or if any closely related persons have such a significant interest. The vast majority of the companies (67.4%) comply with the recommendation, whereas the remaining issuers (32.6%) answered “No”, because no such cases occurred in the period under review.

2.6.2 The BSE considers it important to ensure that more stringent transparency rules are applied to transactions between the company, its subsidiaries and management members and persons closely related to them. Slightly more than half, 51.2%, of companies, declared that they comply with the recommendation. The remaining 48.8% only stated that they did not comply with the recommendation because no such cases occurred during the period under review.

The following recommendation of the BSE, which states that companies are advised to seek approval from the supervisory committee and/or the audit committee for transactions that depart from the above

general practice, is related to the above recommendation. Less than half of issuers, i.e. 41.9%, complied with this requirement. 4.6% said that they complied with the recommendation in part. 53.5% failed to comply with the recommendation. The supervisory committee is informed of such transactions at two of the companies included in this group. Several companies cited the fact that the company does not have a supervisory committee. Others mentioned that their departure from the recommendation was caused by the fact that they had not encountered such cases. Two companies did not provide an explanation.

2.6.3 Furthermore, the BSE considers it expedient for executive body members to inform the supervisory committee/audit committee (nominating committee), if they have received any solicitations for membership in the executive bodies, or management of other companies that are not part of the company group. 69.7% of issuers complied with this recommendation. Several of the 30.3% of issuers that did not comply with the recommendation mentioned that no such solicitations had taken place. In one case, the company stated that a member should inform the Board of Directors of such solicitations and also mentioned that the chairman of the supervisory committee attends the meetings of the Board of Directors as a standing attendee.

2.6.4 The BSE considers it particularly important to ensure that the directors/Board of Directors create the rules of procedure on the flow of information and the management of insider information within the company. The vast majority of companies, 88.3% declared that they comply with the recommendation. Out of the other non-compliant companies (11.7%), in one case this matter was regulated by way of a CEO directive. In another case, a separate rules of procedure was drafted on the management of insider information, but no rules were set out in regards to the flow of information. Another 3 issuers did not make a declaration on the matter.

2.6.5 Based on the recommendation of the BSE, companies are also advised to set out requirements on the securities trading of insiders. 88.3% of issuers complied with the contents of the recommendation. Among companies not complying with the recommendation (11.7%), one issuer partially complied with the recommendation, but did not detail its answer. Another 4 issuers declared that they acted in accordance with the applicable acts of legislation and did not consider it necessary to set out such regulations.

2.7 Performance evaluation, remuneration of the Board of Directors/administrative board, supervisory committee

2.7.1 The directors/Board of Directors is advised to draft remuneration guidelines with regard to the remuneration of the members of the supervisory committee and of management. Substantially less than half, 34.9%, complied with the recommendations. Several of the issuers that did not comply with the recommendation (65.1%) mentioned that in their companies, this task was within the purview of the general meeting. Others have stated that the drafting of such guidelines has not been necessary so far; they did not think that these guidelines should be drafted, either because no such remuneration occurred or because remuneration is determined on a different basis, e.g. it depends on consideration or is not performance-based.

The BSE's recommendation for the supervisory committee to provide an opinion on these directives is also related to this. Even fewer issuers, 32.5%, complied with this recommendation. The remaining 67.5% of issuers cited several different reasons. There were some that mentioned that their companies did not have a supervisory committee. Several issuers noted that they do not have such directives, and there were others that mentioned that these tasks were not within the purview of the supervisory committee.

The BSE's proposal stating that the general meeting should approve the remuneration principles of the administrative board/Board of Directors and that of the supervisory committee in a separate agenda item is also related to recommendation no. 2.7.1. Only 51.2% of issuers complied with this recommendation, while the remaining issuers (48.8%) failed to do so citing various reasons. Many issuers noted that this is not an issue that belongs within the exclusive competence of the general meeting, and some issuers mentioned that the general meeting only decides on the extent of the remuneration but not on the principles on the basis of which that remuneration is provided. Several issuers have mentioned the lack of remuneration guidelines. There are some issuers that did not provide an explanation, while others have mentioned that they did not have a separate remuneration system. It should be noted that for any joint stock companies traded publicly in accordance with the Civil Code, the long-term remuneration and the definition of the incentive programmes of senior executive officers, members of the supervisory committee and employees in leadership roles falls within the exclusive purview of the general meeting, therefore, the statutory provision partially overlaps with the recommendation.³

2.7.2 The administrative board/Board of Directors should evaluate its own performance during the business year in question. The majority of issuers, 79%, complied with this recommendation of the BSE. The other companies (21%) either mentioned that no such evaluation had occurred, or stated that this is not a matter that is within the purview of the administrative board/Board of Directors; and several companies made a promise to comply with this recommendation in the future.

2.7.2.1 The supervisory committee should also evaluate its own performance during the business year in question. 71.4% complied with this recommendation. The remaining 28.6% cited several different reasons, among them the lack of a supervisory committee, and the fact that they would comply with the recommendation in the future.

2.7.3 Controlling the performance of and establishment of the remuneration for the executive management falls within the competence of the administrative board/Board of Directors. 74.4% complied with the recommendation; 4.6% partially complied with the recommendation, while the remaining companies departed from the recommendation, mainly citing reasons of a lack of purview.

2.7.4 Approval should be sought from the general meeting in terms of the principles of stock-based remuneration arrangements. 37.2% complied with the recommendation; while the remaining 62.8% of issuers stated that no such remuneration arrangement exists in their companies.

Prior to the above decision, the shareholders must be informed in detail. Interestingly, more issuers complied with this recommendation (41.9%), even though in principle they do not use such remuneration arrangements. Companies that do not comply with the recommendation (58.1%) have mentioned the lack of such an arrangement as the reason explaining their departure from the recommendation.

2.7.7 The company prepared the remuneration declaration and tabled it to the general meeting. Only 44.2% complied with this recommendation, while the remaining 55.8% did not comply, saying that they did not have such an arrangement or such arrangements did not fall within the purview of the general meeting.

The remuneration declarations must contain the remuneration of the administrative board/Board of Directors, supervisory committee, and management. 53.5% did not comply with this recommendation citing the above reasons, while 46.5% of the issuers complied with the recommendation.

³ Section 3:268 (2) of Act IV of 2013 on the Civil Code.

2.8 The System of Internal Controls and Risk Management

2.8.1 A large majority of the issuers complied with the BSEs recommendations on risk management (namely that the administrative board/Board of Directors or the committees operated by it are responsible for the supervision and management of the entirety of the company's risk management): 90.6%; the Administrative Board/Board of Directors reviews the effectiveness of risk management procedures at a pre-identified frequency: 83.7%; the administrative board/Board of Directors took the necessary steps to identify the most important areas of risk: 93%), Explanations for the few negative answers vary: the supervisory committee is responsible for the topic, the company performs no such activity, or there are no risk management policies.

2.8.2 Close to three quarters (73.8%) of issuers complied with the risk management-related proposal, according to which it is recommended that the administrative board/Board of Directors develop its fundamental risk management principles and fundamental rules of risk management in cooperation with those executives who are responsible for the design, maintenance and control of risk management procedures and their integration into the company's daily operations.

2.8.3–2.8.5 The level of issuer compliance with recommendations on the general issues of internal controls is relatively high. The administrative board/Board of Directors of more than three quarters (76.7%) of issuers developed the principles related to the system of internal controls. The system of internal controls developed by management of 86% of BSE issuers ensures the management of the risks inherent in the business activity of the companies, and the attainment of their corporate objectives. 81.3% of issuers stated that their administrative board/Board of Directors took the aspects featured in the Corporate Governance Recommendations of the BSE into consideration during the development of their internal control system. At 83.7% of issuers, it is the management's task and responsibility to establish and maintain a system of internal controls. There were several explanations that mentioned the size/lack of the business organisation of or the company itself.

2.8.6–2.8.8, 2.8.11 The level of compliance of BSE issuers was significantly lower for questions requesting a more detailed, content- or process-related account of internal controls: less than half of issuers complied with any of the recommendations. Only 37.2% of issuers created an independent internal control function that reports directly to the audit committee/supervisory committee. Only 34.8% of issuers complied with the recommendation that requires the internal audit group to submit a report to the audit committee/supervisory committee at least once a year on the operation of the risk management, internal control, and corporate governance functions. Only less than one quarter of issuers (23.2%) said that internal audit and internal audit activities were conducted based on a mandate from the audit committee/supervisory committee. The same ratio complied with the recommendation according to which internal audit should be organisationally separated from management in charge of operating tasks. The internal audit plan was approved by the company's administrative board/Board of Directors (supervisory committee) based on a recommendation from the audit committee at approximately one third (34.8%) of issuers. 41.8% of issuers stated that it was the administrative board/Board of Directors that prepared the report on the status of the operation of internal controls for shareholders. 39.5% of issuers provided an affirmative answer to the recommendation according to which the administrative board/Board of Directors should develop its procedures on the receipt, processing of reports compiled on the status of the operation of internal controls, and on the preparation of its own related report. Nearly half of issuers (48.8%) stated that their administrative/Board of Directors identified a significant shortcoming in the internal control system and conducted a review and assessment of the related activities as a result.

2.8.10 Pertaining to the recommendation related to the more detailed, content- and process-related issues of internal controls, 60.4% of BSE issuers complied with the recommendation, which advises

that the company's administrative board/Board of Directors take the aspect featured in the Corporate Governance Recommendations of the BSC into consideration for the evaluation of the company's internal control system.

The explanations for the negative responses provided for questions related to the more detailed, content- and process-related issues of internal controls are mostly related to the assertion that the size of the company does not require compliance; no business organisation exists that would need to be controlled; management performs the internal control function, and/or that the issuer does not have an organisational unit responsible for internal control.

2.8.12 Nearly half of issuers (48.8%) complied with the recommendation that a company's auditor should survey and evaluate the company's risk management systems and the risk management activities of company management, and submit the related report to the audit committee/supervisory committee.

2.9 External Advisor, Auditor

2.9.1 Part of the proposals related to the topic are related to the recommendation that the rules of procedure for bodies/committees should contain provisions on the procedure to be followed if the services of an external advisor are used. The rate of compliance in respect of the various bodies and committees was low, in all cases below one third:

- Administrative Board: 32.5%,
- supervisory committee: 32.5%,
- audit committee: 30.2%,
- nominating committee: 6.9% (the typical explanation for “No” answers is that no such committee is in place at the company),
- remuneration committee: 6.9% (the typical explanation for “No” answers is that no such committee is in place at the company).

2.9.2 Only slightly more than half of BSE issuers (53.4%) complied with the recommendation pursuant to which the administrative board/Board of Directors, supervisory committee, and the audit committee are notified in every case when the engagement of the auditor, due to the nature of the engagement, would potentially create significant cost implications, result in conflicts of interest or impact business in any other significant way. The negative answers provided typically related to the fact that no events that would trigger the notification specified in the recommendation occurred in the period under review.

2.9.3 37.2% of issuers complied with the BSE recommendation, pursuant to which the administrative board/Board of Directors must notify the supervisory committee that it engaged the business association or external expert performing the audit in relation to an event that materially affects the company's operation. The typical explanation for non-compliance was that no such event occurred or no such assignment was given at the company, or that there is no supervisory committee in place at the company. One quarter (25.5%) of issuers complied with the recommendation that states that, in its resolution, the administrative board/Board of Directors should record in advance what events may be considered as materially affecting the company's operation. Among negative responses, several cited the fact that there was no such decision, or that the managing body acts in line with its rules of procedure. In the case of an issuer active in the insurance sector, the company referred to sector-specific legal regulations (Act on Insurance).

2.9.4 At the same time, issuer compliance was high (79%) with the recommendation by which the administrative board/Board of Directors should invite the Company's auditor in an advisory capacity to the meetings where the board discusses the agenda items of the general meeting.

2.9.5 Slightly fewer issuers, but still a vast majority (74.4%) complied with the recommendation that states that the internal audit cooperates with the auditor in the interest of the successful completion of the audit.

3.1 Committees: General Principles

3.1.2 Regarding the audit committee, the nominating committee and the remuneration committee, the Corporate Governance Recommendations set forth that the chairman of the relevant committee provide regular information to the administrative board/Board of Directors on certain meetings of the committee, and that the committee prepare at least one report for the managing body and the supervisory committee in the given business year. Regarding the audit committee, which is also regulated the Civil Code, the compliance of issuers is logically higher (72%) than – indicated as explanations for “No” answers – regarding the nominating committee and the remuneration committee, which companies put in place significantly less frequently (slightly less than one third of issuers gave “Yes” answers).

3.1.4 Compliance with the recommendation on committee members having appropriate and suitable skills, expertise and experience is also almost complete (97.6%) The relevant recommendation did not set out requirements or competencies, which could explain the high rate of compliance. The level of compliance with the recommendation on the content of the rules of procedure of committees is relatively high (76.7%).

3.1.6 In respect of the audit committee, the nominating committee and the remuneration committee, the Corporate Governance Recommendations set out proposals that the company publish on its website the tasks delegated to the audit committee, the objectives of the committee, its rules of procedure and composition (indicating members' name, short biography and time of appointment). Regarding the audit committee, which is also regulated the Civil Code, the compliance of issuers is logically higher (55.8%) than – indicated as explanations for “No” answers – regarding the nominating committee and the remuneration committee, which companies put in place less frequently (slightly less than one fourth of issuers gave “Yes” answers).

3.2 Audit Committee

3.2.1–3.2.4 The tasks of the audit committee are set out in the Civil Code and presumably this is the reason why the compliance of BSE issuers in matters related to the audit committee is relatively high, over two thirds of all issuers (and even higher in the premium category):

- 72% of issuers comply with the recommendation that stipulates that the audit committee/supervisory committee supervise the efficiency of risk management, the operation of the internal control system and the activity of internal audit (the explanation for some of the negative responses was that this activity is performed by the Board of Directors, while in other cases negative responses cited internal organisational reasons, e.g. size of the company, absence of an internal audit unit),
- compliance is almost complete (97.6%) among issuers with the recommendation that states that the members of the audit committee/supervisory committee must receive comprehensive

and full information on the unique features of the company's accounting, finances and operation.

- 69.7% of issuers comply with the recommendation stating that the audit committee/supervisory committee has received accurate and detailed information on the audit programme of the internal auditor and the independent auditor; and has received the auditor's report on irregularities uncovered during the audit (the explanation for the majority of negative answers is that there is no internal auditor at the company);
- 67.4% of issuers comply with the recommendation that stipulates that the audit committee/supervisory committee request the new auditor candidate to submit the disclosure statement (the explanation for some of the negative responses was that there was no new auditor candidate at the company).

3.3 Nominating Committee

3.3.1 Very few BSE issuers have a nominating committee in place: among the 43 publicly traded companies, only five premium- and two standard-category issuers (16.2% of all issuers) gave a positive answer to whether there is a nominating committee in place. The reasons for the differences are typically the following: the Administrative Board is responsible for this task, nominations are made by shareholders, the size or activity of the company does not make this necessary or it is not set out by legal regulations. Only a few issuers declared within their corporate governance report that they will examine the possibility of setting up a nominating committee by a given deadline. There are issuers that operate the nominating and remuneration committees as a merged committee, and there have been cases where the nominating committee convened only temporarily.

3.3.2–3.3.4, 3.3.5 The responses given to questions pertaining to tasks performed by the nominating committee feature slightly more “Yes” answers, because certain issuers, approaching questions from the content side, answered “Yes” even if the given activity – in the absence of a nominating committee – is performed by another corporate body. There were issuers that in the absence of a nominating committee gave an answer of “N/A” to these questions. The corporate governance reports also reveal that, among companies where a nominating committee has been put in place, the majority of the companies concerned gave a positive response to questions related to its operation. For issuers active in the banking sector, certain nomination-related matters are governed by sector-specific legal regulations (ACIFE).

3.3.4 Respecting the composition of the nominating committee, the Corporate Governance Recommendations propose that the majority of nominating committee members should be independent. In relation to this particular proposal, four premium- and two standard-category issuers (13.9% of all issuers) declared that the majority of the members of the nominating committee are independent.

3.4 Remuneration Committee

3.4.1 Only very few BSE issuers have a remuneration committee in place: among the 43 publicly traded companies, only five premium- and one standard-category issuer (13.9% of all issuers) gave a positive answer to whether there is a remuneration committee in place. The reasons for the differences are typically the following: the Administrative Board is responsible for this task, such matters are decided on by the general meeting, the size or activity of the company does not make this necessary or it is not set out by legal regulations. Only a few issuers declared within their corporate governance report that they will examine the possibility of setting up a remuneration committee by a given deadline. There are issuers that operate the nominating and remuneration committees as a

merged committee, and there have been cases where the remuneration committee convened only temporarily.

3.4.2–3.4.5 The responses given to questions pertaining to tasks performed by the remuneration committee feature slightly more “Yes” answers, because certain issuers, approaching questions from the content side, answered “Yes” even if the given activity – in the absence of a remuneration committee – is performed by another corporate body. There were issuers that, in the absence of a remuneration committee, gave an answer of “N/A” to these questions. The corporate governance reports also reveal that, among companies where a remuneration committee has been put in place, the majority of the companies concerned gave a positive response to questions related to operation (with the exception of the case of drawing up the remuneration statement, as the remuneration committee only prepares this at three issuers). For issuers active in the banking sector, certain nomination-related matters are governed by sector-specific legal regulations (ACIFE).

3.4.6–3.4.7 Pertaining to the composition of the remuneration committee, the Corporate Governance Recommendations contain one proposal (the remuneration committee is made up solely of non-operative members of the Administrative Board / Board of Directors) and one recommendation (the majority of remuneration committee members should be independent). Compliance with the recommendation on majority members corresponds to the answers given on the establishment of the committee, while only three premium- and two standard-category issuers (11.6% of all issuers) comply with the recommendation on full membership.

3.5 Merging Committees

3.5.1 The nominating committee and the remuneration committee had been merged at two premium- and one standard-category issuers, that disclosed the reasons for merging, in other words compliance in the relevant – otherwise narrow – group is complete.

3.5.2 Of BSE issuers, 12 publicly traded companies (nyrt. – 27.9% of all issuers) released information stating that the Administrative Board/ Board of Directors is responsible for performing the tasks of the nominating committee and the remuneration committee. The reason for the majority of negative responses is structural in nature (i.e. these tasks are not performed by the Administrative Board/Board of Directors), but in some cases, although the explanation is factual (e.g. no information is provided in case of matters regarding the general meeting, the company’s shareholder composition, structure or size does not make the releasing of such information necessary), it clearly does not help shareholders, investors and other stakeholders in clarifying the actual reason for the discrepancy.

4. Transparency and Disclosure

4.1.1, 4.1.3 The vast majority of BSE issuers (72%) drew up disclosure guidelines on the basis of the recommendation setting out such guidelines. The general justification of non-compliance is that the given issuer acts in conformance with legal regulations, BSE regulations and supervisory resolutions. Among issuers preparing disclosure guidelines,

- the majority (21 issuers) complied with the applicable recommendation of the BSE,
- fewer (11 issuers) only informed shareholders in the annual report on the results of the company’s examination relating to the efficiency of disclosure processes,
- the majority (27 issuers) elaborated on electronic, online disclosure processes in their disclosure guidelines.

4.1.2 Irrespective of share category, all issuers ensured that, as part of information provision, all shareholders and market players are subject to equal treatment and that the company's website is designed taking disclosure aspects and the objective of providing information to investors into account.

4.1.4 The survey aimed at the efficiency of disclosure processes was carried out by the vast majority of issuers (86%).

4.1.6 The compliance of premium-category issuers is complete, while 79% of all issuers comply with the recommendation that the administrative board/Board of Directors, in its annual report and on its website, inform the public of its strategic objectives, as well as its policies on its core activity, business ethics and other stakeholder parties.

4.1.7 All premium-category issuers and 79% of all issuers comply with the recommendation on preparing the company's financial statements in line with International Financial Reporting Standards (IFRS).

4.1.8 Less than half, only 44% of issuers, comply with the recommendation that the Administrative Board/Board of Directors should, in the annual report, disclose the nature and size of any other assignments given to the auditing firm in charge of auditing the annual financial statements/reports by the company or its subsidiary. The reason behind some of the "No" answers is that in the given period, there were no such assignments.

4.1.9 65.1% of issuers complied with the recommendation that the administrative board/Board of Directors, in its annual report and on its website, publish information on the professional careers of members of the administrative board/Board of Directors, supervisory committee and management. The explanation for most negative answers is that the given information is not published on each forum.

4.1.10 65.1% of issuers complied with the recommendation that the company disclose information on the internal organisation and operation of the administrative board/board of directors and the supervisory committee. In many cases, the explanation for non-compliance is that the company does not publish separate information as this information is already contained in one of the company documents (e.g. Statutes, rules of procedure of executive bodies). Less than half (39.5%) of issuers comply with the recommendation that the company provide information on the aspects taken into account when evaluating the work of the administrative board/Board of Directors and management as well as the individual members thereof. The explanation for many negative answers was that this information is available to the public as part of the annual general meeting process.

4.1.11 Less than half (41.8%) of issuers gave positive answers to the recommendation, according to which the company, in its annual report and in a remuneration declaration published on its website, should inform the public of the remuneration rules applied, in particular of the remuneration of the members of the administrative board/Board of Directors, the supervisory committee and management. The explanation for the majority of negative answers was that the given issuer does not have remuneration policies in place, and the issuer only publishes information set out in legal regulations, and does not disclose data on remuneration provided to management.

4.1.12 Close to half (48%) of issuers complied with the recommendation that the administrative board/Board of Directors must publish its risk management policies (details on the system of internal controls, the risk management principles applied and their fundamental rules and key risks). The

typical explanation for negative answers was that the company only discloses data that is required by legal regulations. Some answers indicated that the drafting of the new regulations is in progress.

4.1.14 The majority (60.4%) of issuers comply with the recommendation pursuant to which the guidelines relating to the trading of the company's shares and securities by insiders must be published on the company's website. The most frequent explanation of non-compliance was that the issuer complied with the provisions of the Capital Market Act in force at the time and has the required internal policy in place. The vast majority (86%) of issuers comply with the recommendation according to which the company, in its annual report and on the company's website, must disclose the shares held by members of the administrative board/Board of Directors, the supervisory committee and management of the company's securities and their involvement in the equity-based incentive system. The main explanations of non-compliance were as follows: there is no equity-based incentive system in place, and/or the issuer only complies with the disclosure of information set out in the legal regulations.

4.1.15 Less than half (48.8%) of issuers complied with the recommendation that stipulates that the company must disclose, in the annual report and on the company's website, all relationships of the members of the administrative board/Board of Directors and management with any third parties that could impact the operation of the company. The explanation for the majority of negative responses was that there were or there are no such relationships.

4.1.5, 4.1.13, 4.1.16 In cases where the legal regulation or the stock exchange regulations cover the applicable recommendation of the BSE in part or in whole, the compliance of all issuers or the issuers belonging to the applicable share category is complete, with one exception:

- All issuers in the premium category comply with the recommendation to disclose the calendar of events on the issuer website, while apart from them, only four standard- and two technical-category companies comply. As a result, overall compliance among all issuers is 41.8%. The reason for this clearly is the fact that pursuant to the BSE'S GBR, "Issuers of Premium Equities are obliged to publish their corporate event calendar by 1 January each year (or by the first day of the business year if a different year from the calendar year is used)".
- With one exception, all issuers comply with the recommendation which states that for the adequate information of market players, simultaneously with the publication of the annual report, the company shall disclose its report on corporate governance. The reason for this clearly is the fact that, pursuant to the BSE'S GBR, "The equity's issuer is obliged to publish its Corporate Governance Report prepared in accordance with the 'Corporate Governance Recommendations', published by the Stock Exchange, concurrently with the disclosure of the annual report".
- All premium-category issuers comply with the recommendation on issuers providing English-language information, while apart from these issuers, only two standard-category companies comply with this recommendation. As a result, compliance among all issuers is 32.5%. The clear reason for this is the fact that, pursuant to the BSE'S GBR, "as the selected language (or as one of the selected languages), issuers listed or classified into the Premium Equities category are obliged to select English".

IV. CONCLUSIONS

1. Summary Conclusions

The Corporate Governance Committee of the BSE

- based on its review of the 2016 corporate governance reports published by the issuers,
- taking the provisions of Commission Recommendation 2014/208/EU into consideration,
- has made the following summary conclusions

in the interest of the appropriate information of shareholders, investors and other stakeholders:

Considering that the issuers, with one exception, have published their corporate governance reports, it can be established that they consider compliance with the recommendation to provide appropriate information to the public important. According to the assessment of the Committee, in the interest of creating a uniform practice going forward (i.e. to ensure uniform quality standards and level of detail of information across all reports, and to avoid the shortcomings experienced in this round), the Committee has issued recommendations.

The Committee calls the attention of the issuers to the necessity of preparing the report specified in Annex 1 to the Corporate Governance Recommendations, and to the substantive and detailed elaboration of all sections therein.

The Committee recognises and appreciates compliance with the individual recommendation and proposal categories, but nonetheless calls on issuers to enhance the level of compliance with content- and process-related expectations, in addition to meeting the associated formal requirements.

The Committee notes that, in the event of departures from the recommendations, it is expedient to present the substantive reasons underlying the departure, describe the measures undertaken in place of compliance and show how those measures lead to compliance with the recommendation or the attainment of the objectives of the recommendation in such a manner that shareholders, potential investors, and other stakeholders are able to appropriately assess the company's corporate governance practices, and make informed decisions regarding their investment. Considering that potential non-compliance does not necessarily in itself mean that a company is adversely regarded, and that the level of compliance of the individual issuers cannot be identical due to industry-specific features and differences in operating practices, with regard to the cases of non-compliance, the Committee reminds issuers that, in their explanation of departures from recommendations, they should also elaborate on how a measure taken in place of compliance contributes to the good corporate governance of the company. The explanation can only fulfil its true purpose if it includes an elaboration of how, even though the objectives specified in the Corporate Governance Recommendations are not implemented using the solutions listed in the Recommendations, they can be attained through solutions that are more suited to the given issuer.

The Committee noted that under certain topics where proposals were more prominent, explanations of departures were less likely to have been included, as explanations of departures from the recommendations are not mandatory.

The Committee acknowledges that levels of compliance for individual committees (remuneration committee and appointment committee) was considerably lower than those

questions related to committees required by law (audit committee). In connection with this, the Committee warns issuers that are not compliant with the relevant recommendations to consider setting up these committees in the interest of the implementation of an appropriate corporate governance practice, or at least elaborate in their explanations in more detail on any solutions that are equivalent to the operation of such committees.

The Committee welcomed issuer explanations that indicated that the issuer is planning to comply with the given recommendation by a specific deadline. In connection with this, the Committee is hoping that the level of compliance in future corporate governance reports – as a result of measures taken in order to improve issuer corporate governance practice – will overall be higher.

Given the legal amendments that entered into force in the meantime, the Committee has put the review of the BSE's effective Corporate Governance Recommendations on its agenda. During the review, the Committee will take the experiences gained during the assessment of issuer reports into account, and call the attention of issuers to typical deficiencies in amended recommendations, with particular emphasis on the full application of the “comply or explain” principle.

In respect of the above principle, it may be stated that in their justification of departures, the issuers provided explanations based on a non-uniform set of considerations. Therefore, the Committee intends to facilitate the improvement of the quality of the reports by issuing a more detailed guidance document.

2. Other general conclusions

Despite drawing the attention of issuers to this problem earlier, during the monitoring of the corporate governance reports by exchange issuers, the Committee observed that, in the cases of certain corporate governance reports,

- numbering and breakdown different from those set out in Annexes 2 and 3 of the effective Corporate Governance Recommendations were applied, which means that there might be technical difficulties in comparing corporate governance reports;
- the responses to recommendations and proposals were missing;
- the explanations for “No” answers given to recommendations were missing;
- and for given questions of the recommendation or the proposal, instead of “yes”/“no” answers, “N/A” or “not applicable” was featured.

In order to make the corporate governance reports of issuers comparable by shareholders, investors and other stakeholders, and for these to contain clear and accurate information, the Committee in general asks issuers to

- draw up their corporate governance reports on the basis of the effective Corporate Governance Recommendations, in line with the structure and numbering set out therein;
- answer all sections of the Corporate Governance Recommendations in their corporate governance reports;
- provide explanations for “No” answers given to recommendations (“comply or explain” principle); and
- ensure that their responses are clear (yes/no).