

# Guideline for Board on the Governance of Subsidiaries and Associate Companies



# Content

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<b>03</b>	<b>Introduction</b>
<b>04</b>	<b>Working Committee on ESG Guidelines for Boards 2021</b>
<b>05</b>	<b>Section 1 Key principles</b>
<b>08</b>	<b>Section 2 Guidelines</b>
<hr/>	
<b>09</b>	<b>Guideline 1 Basic understanding about investment in subsidiaries / associate companies</b>
<hr/>	
	<b>Guideline 2 Conceptual framework in governing subsidiaries / associate companies</b>
<b>12</b>	2.1 Applying good governance principles with subsidiaries / associate companies
<b>14</b>	2.2 Governance guidelines for different relationships between parent and subsidiaries / associate companies
<hr/>	
	<b>Guideline 3 Key issues to consider in governing subsidiaries / associate companies</b>
<b>16</b>	3.1 Overall governance structure and mechanism
<b>17</b>	3.2 Board of subsidiaries / associate companies
<b>20</b>	3.3 Qualification consideration and director nomination at subsidiaries / associate companies
<b>21</b>	3.4 Roles, duties, and responsibilities of representative director
<b>22</b>	3.5 Strategy governance
<b>23</b>	3.6 Authority scope of parent and subsidiaries / associate companies
<b>24</b>	3.7 Policy / guideline concerning key matters
<b>25</b>	3.8 Effective communication and disclosure channels
<b>26</b>	3.9 Corporate control / audit mechanism
<b>28</b>	3.10 Items with potential conflict of interest
<hr/>	
	<b>Annex</b>
<b>30</b>	1. Subsidiary, associate company, and relevant definitions
<b>33</b>	2. Observation points for the Board concerning parent-subsidiary relationship
<b>34</b>	3. Initial checklist for the Board in governing subsidiary
<b>35</b>	4. Example of reporting format/framework for subsidiary to propose to parent's Board
<b>36</b>	5. Key issues for evaluation of Board efficiency and readiness to perform duties
<hr/>	
<b>37</b>	<b>References</b>

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# Introduction

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There are several reasons for companies nowadays to invest in subsidiaries / associate companies. For instance, to enhance business strength, to accommodate new corporate strategy, to lift management flexibility through business separation etc. Such investment is one mechanism that facilitates risk diversification, adds income channel, and provides opportunity for sustainable growth.

Since subsidiaries / associate companies are controlled or under material influence of the company, the Board (as organization leader) should recognize the significance and ensure effective performances of those companies to retain utmost benefit of the company as well as subsidiaries / associate companies and other relevant stakeholders.

Given the rationale, governance of subsidiaries / associate companies become one of the hot topics among Boards and personnel in the corporate governance field all over the world. However, there has been but limited knowledge and guidelines in this regard and they had hardly been developed or applied on the international scale. This owed partly to the complexity in shareholding structure, business characteristics, legal context etc. that may differ in each company.

Such complexity has become a challenge for the Board in maintaining proper balance between the “degree of control” of the parent company and “degree of autonomy” of subsidiaries / associate companies to ensure mutual benefits. At the same time, the Board of subsidiaries / associate companies must also comprehend with their challenging corporate governance roles in alignment with policy of the parent company while making decision for utmost benefit of the subsidiary / associate company.

This guideline has been developed to reflect the significance of this matter and the necessity of the Board to have clear governance direction of subsidiaries / associate companies. The IOD sincerely hopes the essence of this document will support the Board in performing its duties and ensure effective mutual responsibilities between the parent, subsidiaries, and associate companies. Knowledge and guidelines provided in this document are not set in stone but the Board should learn from them, comprehend the differences, and apply with the company as deem appropriate.



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### Guidelines for Boards 2021

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Section 1



# Key Principles

## Key Principles

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- 1 The Board should understand “objectives” for the establishment or investment in subsidiaries / associate companies as well as management mechanism, legal context, and relevant risks to be able to determine effective governance direction of those companies. *(See Guideline 1)*
  - 2 The Board should ensure the company and other investors (if any) jointly set governance framework / policy of the subsidiaries / associate companies by maintaining appropriate “degree of control of the parent company” and “degree of autonomy of subsidiaries / associate companies” in accordance with the context and relevant regulations. *(See Guideline 2.1)*
  - 3 The Board should not focus only on building framework / rules between the company and subsidiaries / associate companies to ensure compliance. It should also emphasize performance development of each company on the basis of existing business relationship to enhance sustainability of the whole group. *(See Guideline 2.2)*
  - 4 The Board should accommodate the establishment of “mechanism to integrate key information” to comprehend the overall picture of internal management structure, relationship between the company and subsidiaries / associate companies, organizational culture, business characteristics, and shareholding structure that may differ in each company. *(See Guideline 3.1)*
  - 5 The Board of subsidiaries / associate companies should comprise of persons who possess appropriate qualifications that will benefit business operations of respective subsidiaries / associate companies. They are tasked to steer business operations of those companies to achieve corporate objectives. The Board should appoint persons to assume the role of “representative director” in subsidiaries / associate companies in accordance with shareholding proportion and / or agreements between co-investors. *(if any) (See Guideline 3.2 and 3.3)*
  - 6 The Board of subsidiaries / associate companies should adhere to Fiduciary Duty for the utmost benefit of the subsidiaries / associate companies as well as all stakeholders not just of the parent or any particular group of shareholders. Such roles, duties, and responsibilities should be stipulated clearly in written in the form of “Board Charter”. *(See Guideline 3.2 and 3.4)*
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- 7 The Board should encourage directors or management of the subsidiaries / associate companies to discuss, opine, or present key information concerning business environment and risk factors that may be specific to particular subsidiary / associate company. The information will be considered in reviewing strategy, policy, and long-term objectives of the whole group of companies. *(See Guideline 3.5)*
- 8 The Board should ensure the scope of authority between the company and subsidiaries / associate companies is clearly determined. There should be clear indication on cases that the representative director can use own discretion to vote in the Board meeting of the subsidiaries / associate companies and cases that require prior approval from the Board meeting and/or the shareholders' meeting of the company. *(See Guideline 3.6)*
- 9 The Board should ensure the company and other investors (if any) jointly stipulate key policy to be enforced with subsidiaries / associate companies, which could be the enforcement of Group-Wide Policy. The Board may need to allow the Board of subsidiaries / associate companies to use own discretion in determining certain policy that align with business context and can practically be enforced. *(See Guideline 3.7)*
- 10 The Board should ensure availability of communication mechanism between the company and subsidiaries / associate companies and that it is clear, transparent, accurate, and timely. It should also establish monitoring channel for the Board to see that subsidiaries / associate companies disclose operating information or significant items effectively and timely. *(See Guideline 3.8)*
- 11 The Board should examine to ensure that subsidiaries / associate companies that it invested in have prudent and effective internal control, internal audit, compliance, and risk management mechanisms or systems. *(See Guideline 3.9)*
- 12 In case of connected transaction between companies within the group that may trigger conflict of interest, the Board should ensure that the company and subsidiaries / associate companies comply with "connected transaction policy" as well as approval criteria and procedures on arms' length basis by emphasizing the utmost benefit of the company. *(See Guideline 3.10)*

## Section 2



# Guidelines



## Guideline 1 | Basic understanding about investment in subsidiaries / associate companies

- 1.1** The Board should have adequate knowledge in the definition, relationship, authority structure, legal constraints, and mechanisms concerning the establishment or investment in the subsidiaries / associate companies (Please see additional definitions in Annex 1)
- 1.2** In case the company invests in subsidiaries / associate companies, the Board should ensure the company has clear “mechanism or procedures to consider objectives” of the investment to create common understanding about the rational, condition, or necessity (if any) which may fall into any of the following case:
- 1.2.1 Establish or invest to accommodate corporate strategies such as
    - 1.2.1.1 Risk Diversification to strengthen the company and prevent takeover.
    - 1.2.1.2 Business expansion to create economies of scale.
  - 1.2.2 Establish or invest to promote business activities such as
    - 1.2.2.1 Creating flexibility by separating work divisions such as production, sales, logistics to keep business structure from getting excessively large and obstruct administration.
    - 1.2.2.2 For marketing benefit, making clearer division of client / product segments.
  - 1.2.3 Establish or invest for other objectives such as
    - 1.2.3.1 To accommodate plans to spin off and list on the bourse.
    - 1.2.3.2 For tax benefits and investment incentives from the state.
    - 1.2.3.3 To comply with legal constraints or relevant rules and regulations.
    - 1.2.3.4 To be another channel to make profit or financial returns.

Regardless of investment objectives in subsidiaries / associate companies, the Board should ensure that such investment aligns with vision, mission, and purpose of the company.

### QUESTIONS for BOARD:

- What “opportunity” does the company see that make it invest in the subsidiary / associate company?
- How “necessary” it is to invest or establish the subsidiary / associate company?
- What is the “expected” result from investment in the subsidiary company / associate company and how “worthy” is it?
- How much should the company invest in the subsidiary / associate company and why?

**1.3** The Board should ensure the company has mechanism to consider relevant details such as investment proportion, expected profit, financial status of the company etc. while investment analysis procedures must be appropriate and prudent procedures. It should also see that the investment matches the “investment objectives” (Guideline 1.2) before proposing to the Board and shareholders for approval.

**1.4** The Board may encourage the company to draft “policy for investment in other company” to be used as a framework or broad guideline in considering the matter as deem appropriate. For instance:

1.4.1 The company may have policy to set up or invest in other company with “enough” proportion to gain control or take significant part in managing that company if it considers that business of the investment target relates directly with the company’s business or has high potential to accommodate / support the company’s long-term strategy.

1.4.2 The company may have policy to invest in other company only as financial investment (not aiming to gain controlling stake) if it considers that the main objective is to enhance revenue channel or seek financial return from that company.

However, the consideration must be in accordance with specific condition of each company and industry regulations. For instance, the Board of financial institution must ensure the investment policy aligns with relevant methods / criteria specified in the Bank of Thailand’s announcements.

**1.5** Besides cost-benefit analysis of the investment, the Board should also consider potential “risks” from establishment or investment in the subsidiary / associate company in order to determine risk mitigation measures accordingly. Key risks that the Board should consider include

1.5.1 **Conflict of interest risk:** Particularly in subsidiary with other groups of shareholders. The parent company (with majority vote) may assign the subsidiary do something to accommodate the parent’s policy without taking other shareholders into consideration or not being for the utmost benefit of the subsidiary or its stakeholders.

1.5.2 **Financial risk:** Particularly in holding company because its performance depends on operations of subsidiaries / associate companies. Should any subsidiary / associate company post weaker earnings or face bankruptcy, it would inevitably affect financial status of the company.

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- 1.5.3 **Administration risk:** Especially in company with many subsidiaries / associate companies or that with complex group structure, making it unable to fully monitor all subsidiaries / associate companies and, therefore, cause ineffective operations in the big picture.
- 1.5.4 **Reputation risk:** For example, fraud case by management / employee in subsidiary / associate company could trigger spillover effect on the image of the company.
- 1.5.5 **Risk concerning connected transaction:** Especially in company with many subsidiaries as they may engage in intra-group transaction that are not based on fair and rational condition. Doing so could lead to benefits transfer among themselves, not for utmost benefit for the whole group of companies.
- 1.5.6 **Other risks:** These kind of risk depends on business context of each company. For examples, risks concerning legal complexity and international fund transfer restrictions (in case the company has subsidiary / associate company in other country), risks concerning compliance with criteria for the establishment permission and change in business structure specified in the Bank of Thailand's announcement. (in case the company is a financial institution)

- 1.6** Besides the company's usual financial statement, parent company with investment in subsidiary must also prepare "consolidated financial statement" to present assets, liabilities, shareholders' equity, revenues, expenses, and cashflows of both the parent and subsidiaries as if they are the same entity. For associate company, the company must book the investment by applying the Equity Method.

Given complexity in the preparation of financial statements, the Board should recognize the risks of substantial inaccurate financial information. (either by fraud or operational mistake) It should closely govern and audit to ensure the financial statements are in alignment with the law / accounting standard, accurate, and credible.

- 1.7** Before making decision to establish or invest in subsidiary / associate company, the Board should comprehensively consider both "opportunities" and "risks" (Guideline 1.2-1.6) to ensure the investment is truly for the utmost benefit of the company and stakeholders. This is considered the Board's Duty of Care in accordance with the Fiduciary Duty principle.

## Guideline 2 | Conceptual framework in governing subsidiaries / associate companies

### 2.1 Applying good governance principles with subsidiaries / associate companies

2.1.1 Governing subsidiaries / associate companies is like large corporation that controls and monitors administration of several branches. However, subsidiaries / associate companies differ from branches because they have separate juristic person status and have their own Boards. Therefore, governing subsidiaries / associate companies have certain aspects that should be considered and set as priorities.

2.1.2 The goal in governing subsidiaries / associate companies is not for the parent to interfere and take control (micro-governance) but to establish “governance framework, policy, and process” at appropriate level. Doing so is meant to ensure business direction alignment of the whole group, not letting each subsidiary / associate company govern themselves in their own different directions and not for the utmost benefit of the group.

#### Key goals in governing subsidiaries / associate companies

1. To create control mechanism and monitor that operations of subsidiaries / associate companies align with corporate governance principles as well as relevant rules and regulations.
2. To create channels to communicate, exchange, and disclose information between the parent- subsidiaries / associate companies in effective and timely manner.
3. To create operating guideline of subsidiaries / associate companies that aligns with goals and policies of the parent for the utmost benefit of the whole group.
4. To create transparency in operations of subsidiaries / associate companies by ensuring no transaction that may trigger conflict of interest or unfair treatment against stakeholders.

2.1.3 Key challenge of the Board is how to create framework, policy, and process in governing subsidiaries / associate companies that can still maintain balance between the degree of control and degree of independence at optimum level for each company?

- 2.1.4 The framework in governing subsidiary can roughly be divided into two models depending on the scope of decision-making authority.
- 2.1.4.1 Centralized Governance Model – The parent has direct role in controlling operations of the subsidiary as if it is a “unit” of the parent. Most decision-making authority depends mainly on policy / discretion of the parent.
- 2.1.4.2 Decentralized Governance Model - Subsidiary can govern and control its own operations while being able to decide freely on most matters by ensuring they align with the parent’s direction.
- 2.1.5 The Board should observe and consider pros and cons as well as other constraints of the two governance models.
- 2.1.5.1 Although “centralized” governance ensures that operations of subsidiary align completely with objectives of the parent, the model may be obstacle for company with complex structure or have numerous subsidiaries because the parent may not be able to take full control of all subsidiaries.
- 2.1.5.2 Although “decentralized” governance ensures that operations of subsidiary match its context, allowing flexible and effective business management, and reduce monitoring burden of the parent, it could ignite risk that each subsidiary operate in their own direction that may not align with benefits of the parent.
- 2.1.6 Practically, the Board may use both models by applying the right mixture as deem appropriate. For example, the Board may apply “centralized” model with subsidiaries that it deem to be small or have direct business linkage with the parent or in business that the parent has expertise. On the other hand, the Board may apply “decentralized” model with sizable subsidiaries that require substantial resources / investment or subsidiaries that are already listed / have plan to list on the bourse or conduct complex business and different from that of the parent etc.

However, the guideline above is not one size fits all solution for all companies. Therefore, the Board should consider model that match the company’s context as well as relevant rules and regulations.

- 2.1.7 In case there is other investor in the subsidiary or associated company, the scope of controlling authority and degree of management independence will be determined in the agreement among shareholders / companies with joint controlling authority or in the “shareholders’ agreement.” However, the determination must comply with the relevant laws, rules, and regulations.

## 2.2 Governance guidelines for different relationships between parent and subsidiaries / associate companies

- 2.2.1 In governing subsidiaries / associate companies, the Board should not emphasize only on the formation of framework / rules for compliance but should also focus on the performance of subsidiaries / associate companies, based on existing business relationship to create synergy and lead to sustainable growth for the whole group.
- 2.2.2 Business relationship structure between the parent and subsidiaries / associate companies could be in different forms such as (1) One party depends greatly on the other. For examples, the parent may be major client of the subsidiary / associate company (unit depends on parent) or subsidiary / associate company may be major supplier of the parent (parent depends on unit) etc. (2) Parent and subsidiary / associate company depend greatly on each other, possibly by being major clients of each other. (3) Both the parent and subsidiaries / associate companies engage in businesses that do not depend on each other. The subsidiaries / associate companies are like elements in the business portfolios that meant to generate other revenue channel for the parent. (4) Other forms of relationship in accordance with context of each company.

Such relationship structure could bring about different business “opportunities” and “threats.” Therefore, the Board should prudently observe and consider these issues to determine appropriate management direction by ensuring the existence of any subsidiary / associate company will not cause business damage or deteriorate the parent’s strength. (See Annex 2)

- 2.2.3 The Board should bear in mind that any business relationship could transform and, therefore, it should constantly review the relationship to understand if it has transformed and how in order to set appropriate governance framework (both in terms of performance and compliance) in alignment with such transformation.

2.2.4 Number of subsidiary / associate company could accumulate over time and eventually make internal structure more complex and difficult to control. Therefore, the Board should ensure the company periodically conduct efficiency assessment of the group's management structure and make adjustment as deem appropriate. For example, the Board may divide businesses into core business and non-core business by taking into consideration potential, strategic significance, and future growth opportunity of each business. Doing so will create structural clarity, which will lead to appropriate determination of the parent's degree of control and decision-making authority in companies of each business group. (Core / Non-Core) It can also enhance resource allocation efficiency within the group, which could directly affect the capability to achieve the company's long-term goals.



## Guideline 3 | Key issues to consider in governing subsidiaries / associate companies

The Board should set appropriate governance framework and mechanism in governing subsidiaries / associate companies to ensure transparent and verifiable management for the company's benefits. Key issues that should be taken into consideration are listed below:

### 3.1 Overall governance structure and mechanism

3.1.1 The Board should ensure the company has clear and concrete plan, process, or mechanism to govern subsidiaries / associate companies so that relevant persons can use as a guideline while it can also be used to create understanding with stakeholders. The substance should cover overall process from the determination of establishment objectives, registration, management, transformation, and termination of subsidiary / associate company.

3.1.2 The Board should comprehend with management structure, corporate culture, business characteristics, shareholding structure, and relationship between the company and subsidiary / associate company etc. to promote the holistic view.

#### QUESTIONS for BOARD:

- How will the establishment / termination of subsidiary / associate company affect business direction, management structure, and earnings of the group?
- What are "indicators" for the establishment, additional investment or, termination of the subsidiary / associate company?
- Does the company currently have appropriate number of subsidiaries / associate companies that allow effective control?...What are the company's long-term plan on this matter?

3.1.3 In case the company has subsidiary / associate company in other country, the Board should recognize regulatory issues that may differ from the parent company (e.g. determination of Board composition etc.) and ensure it complies with laws and sociocultural context of the local jurisdiction.

3.1.4 The Board should encourage the company to set up mechanism to store, compile, and integrate key information of subsidiaries / associate companies. It could be in the form of "Central Database" that can be accessible by Board members and/or the management.



- 3.1.5 The Board should ensure the company has Governance Risk management guideline to accommodate effective control over operations within the group. It may set broad consideration criteria that covers 1) establishment of a new company 2) change in management structure of existing company and 3) termination of company that is either not making profit, not conducting business, or already achieving objectives of the establishment.
- 3.1.6 The Board should encourage the company to disclose information concerning how it govern subsidiaries / associate companies as well as key information of those subsidiaries / associate companies (even if they are not listed) to inform stakeholders properly and adequately, which will enhance transparency and uplift governance standard.

## 3.2 Board of subsidiaries / associate companies

- 3.2.1 The Board of subsidiaries / associate companies should comprise of persons with knowledge, expertise, and experience that are useful for the subsidiaries / associate companies to control and determine management policy in accordance with stipulated objectives, rules and regulations, and corporate governance principles.
- 3.2.2 Board structure and composition of subsidiaries/associate companies usually comprising
- 3.2.2.1 Director that represents a group of shareholders or “representative director”, who are appointed to protect benefits of that group.
  - 3.2.2.2 Independent Director, who may be appointed in accordance with regulatory requirement (in case the subsidiary / associate company is a listed company) or for other objectives (e.g. to comply with corporate governance guideline or to protect benefits of retail shareholders).
  - 3.2.2.3 Other directors. If the subsidiary / associate company conducts business overseas, it may be legally required to recruit persons who understand the context or business pattern in that country (usually local resident) to join the Board.

- 3.2.3 For wholly-owned subsidiary, the Board's size, structure, and composition of the subsidiary is subject to discretion of the parent. In such case, the size and business complexity as well as relevant regulations and specific industry condition of the subsidiary should be taken into account.
- 3.2.3.1 In case the subsidiary is not a listed company, all Board members could be the parent's directors, management, or persons related to the parent. (Practically, there are common directors who sit on the Board of both parent and subsidiaries at the same time) This is a popular method used by companies that emphasize "centralized governance" model because it accommodates close monitoring of the subsidiary's operations.
- 3.2.3.2 The Board should be cautious that if most (or all) directors of the subsidiary are personnel of the parent, it may lead to imbalanced governance aspects. Such case could also create work environment that is too much "like the parent" or "for the parent" and make the Board overlook duties "for the subsidiary and stakeholders."
- 3.2.3.3 Although the subsidiary is not listed, the Board could still consider nominating "independent directors" in the subsidiary's Board. This method matches with parent that emphasizes on "decentralized governance" model, authorizing the Board of subsidiary to make decisions to a certain extent. This is another way to promote effective check & balance mechanism and enhance transparency of the subsidiary's Board to ensure utmost benefits of all stakeholders, not just of the parent.
- 3.2.3.4 Independent director at the parent is entitled to be appointed "non-executive director" or "independent director" of the subsidiary. However, if the director is also a member of the parent's "audit committee" and the subsidiary is a listed company, the director is not qualified to be director of the subsidiary. Each listed company has its own shareholders that require audit committee to protect benefits of the shareholders. (particularly retail investors) If a member of the parent's audit committee also assume directorship at the subsidiary, it could trigger conflict of interest.

The Board should consider this matter with cautious by assessing the ability to maintain "independence" in performing duties as independent directors. (at both the parent and subsidiary)

<sup>1</sup> Although the law does not prohibit independent director, who are member of the parent's "audit committee", from assuming the role of "non-executive director" or "independent director" at unlisted subsidiary. The guideline does not consider it to be "good practice."

<sup>2</sup> Source: "FAQ roles and duties of the Board" โดยสำนักงาน ก.ล.ต. (<https://www.sec.or.th/cgthailand/th/pages/faq/bodfaq.aspx#sec4>)

- 3.2.4 In case there is other investor in the subsidiary or associated company, the determination of Board composition will be in accordance with the agreement among investors or the “shareholders’ agreement.” However, the determination must comply with the relevant laws, rules, and regulations. Normally, companies usually have a policy to nominate representative to join the Board in accordance with the proportion of share ownership in that subsidiary. In case the subsidiary is a listed company, relevant rules and regulations must also be taken into account.
- 3.2.5 Authority, duties, and responsibilities of the subsidiary’s / associate company’s Board in each group of companies may vary. They could be restricted or set at narrower scopes than those of the parent’s Board depending on circumstances and relevant conditions such as:
- 3.2.5.1 Controlling authority of the parent. (full or partial ownership)
  - 3.2.5.2 Status of the subsidiary / associate company. (company limited or listed company)
  - 3.2.5.3 Specific industry regulations / conditions or country that the subsidiary / associate company operates.
  - 3.2.5.4 Agreement between the parent, company with joint controlling authority, or other investors.
  - 3.2.5.5 Other factors such as the parent’s decentralization policy, business connection with the parent, business complexity of the subsidiary / associate company.
- 3.2.6 Roles, duties, and responsibilities of the subsidiary’s / associate company’s Board has special characteristic called Dual Duty. Besides the usual roles as the Board of any company that include control & monitoring to ensure the management run the company in accordance with objectives for the utmost benefits of the subsidiary / associate company, the Board of subsidiary / associate company is also “key linkage” (both in terms of relationship and policy) with the parent and other subsidiaries / associate companies (if any). It is considered a mechanism that promote coordination and integration within the group.
- 3.2.7 Roles, duties, and responsibilities of the subsidiary’s / associate company’s Board should be stipulated clearly in written in the form of “Board Charter” and should be reviewed at least annually. There should also be regular assessment of efficiency / readiness to perform duties, particularly in issues with “specific context” of the subsidiary’s / associate company’s Board. (See Annex 5)
- 3.2.8 The Board of subsidiary / associate company should adhere to Fiduciary Duty for the utmost benefit of the subsidiary / associate company as well as all stakeholders, not just for the benefits of the parent or specific group of shareholders.

### 3.3 Qualification consideration and director nomination at subsidiaries / associate companies

- 3.3.1 The Board should nominate director (“representative director”) to control and take part in setting policies of the subsidiary / associate company to ensure they align with objectives and comply with regulations and corporate governance principles.
- 3.3.2 In recruiting representative director for subsidiary / associate company, the Board should consider various aspects such as having no interest in the company, leadership, knowledge, competency, and experiences that are useful for business operations. The representative director may be recruited from any Board member or management of the company (some company stipulates minimum position such as “assistant vice president”) or external person who has skill and expertise that will benefit the subsidiary / associate company.
- 3.3.3 In recruiting representative director for subsidiary / associate company, the Board should also consider specific conditions of each subsidiary / associate company such as
- 3.3.3.1 Complexity in business operations of the subsidiary / associate company.
  - 3.3.3.2 Under complex or risky regulations such as being public company that list on stock exchange (locally or abroad).
  - 3.3.3.3 Regulations applied in country that the subsidiary / associate company operates or establishes.
- 3.3.4 In case the company nominates its executive to be director of subsidiary / associate company, the Board should ensure that executive has adequate comprehension with the different hats and switching roles between “manage” and “govern.”
- 3.3.5 In case there are several subsidiaries / associate companies, the Board should ensure representative directors do not assume directorship at too many subsidiaries / associate companies at the same time because it could cause too much burden and prevent effective performance. The Board may set “maximum” positions as deem appropriate. For example, the Board may stipulate that any representative director can take Board seats at no more than xx subsidiaries / associate companies.
- 3.3.6 The Board may assign the CEO to appoint representative director should it deem that the subsidiary is a small operating arm of the company.
- 3.3.7 The parent’s Board should evaluate performance of representative director annually and make it part of the consideration in future nomination of that person as director at subsidiary / associate company.
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- 3.3.8 In appointing CEO or senior management of the subsidiary / associate company, the Board may set guideline by assigning a representative from the parent company (e.g. a director) to participate in the consideration process or it may give the Board of subsidiary / associate company freedom to use its discretion. There is no fixed format and practices may vary as deemed appropriate or in accordance with agreement between the company and other investors. (if any)

### 3.4 Roles, duties, and responsibilities of representative director

- 3.4.1 The Board should stipulate roles, duties, and responsibilities of representative director which usually cover the following issues:
- 3.4.1.1 Perform duties with care, responsibility, honesty, and in accordance with objectives, regulations, and resolution of the Board or shareholders of the subsidiary / associate company as well as relevant laws.
  - 3.4.1.2 Provide guideline in determining strategic direction, policy, and business plan of the subsidiary / associate company to align them with the parent's direction. Some company may stipulate that representative director must seek (advance) guidance from the parent before expressing views in the Board meeting of the subsidiary / associate company, especially when the meeting has crucial agenda in the strategic / policy level that could yield material impact.
  - 3.4.1.3 Monitor and report the parent about operations of the subsidiary / associate company as well as inform the parent immediately should the subsidiary / associate company plan to engage in any transaction that requires disclosure to the regulatory body.
  - 3.4.1.4 Consider and vote at the Board meeting of the subsidiary / associate company in issues concerning general operations as deemed appropriate by using own discretion freely to preserve benefit of both the parent and subsidiary / associate company. The representative director must also stand ready to object in good faith should there be different views than other directors.
- 3.4.2 Representative director is nominated to preserve benefits of the parent's investment by taking actions in accordance with assigned policy framework. Should the representative director find that doing so may not be for the utmost benefit or contradict with objectives of the subsidiary / associate company, the director should report to the parent immediately to seek appropriate resolution. Meanwhile, the parent's Board should also have fair and rational mechanism to consider such conflicting case which will encourage the representative director to fully perform fiduciary duty in governing the subsidiary / associate company.

### 3.5 Strategy governance

3.5.1 Companies that emphasize centralized governance model usually stipulate that subsidiary adopt objectives, business strategy, risk appetite, and budget that already approved by the parent' Board from the beginning to ensure alignment with the whole group. Therefore, it is not unusual for the subsidiary's Board to have limited roles and discretion or narrower scope of authority than the Board of companies in general.

3.5.2 Although the parent is tasked to determine overall strategic direction for the subsidiary to adopt, the Board should encourage collaboration mechanism between parent and subsidiary in reviewing strategic direction periodically in accordance with the context of each company.

3.5.3 Companies that emphasize decentralized governance model may allow the subsidiary to determine its strategic direction and business plan freely by ensuring the strategic plan aligns with the parent's risk appetite and does not contradict the parent's objectives and business goals. This can be implemented in various ways as appropriate such as

3.5.3.1 Conduct a strategic session with representative directors of subsidiaries to discuss and create common understanding about the parent's policy and overall business direction of the whole group.

3.5.3.2 Stipulate that subsidiary must propose strategy draft to the parent's Board for approval before putting into implementation.

3.5.3.3 Set requirement that representative from the parent join the subsidiary's strategy development process.

These methods could empower subsidiaries and drive them to explore business opportunities while enhancing strategic potential without competing for resources or igniting cannibalization among each other. Meanwhile, the parent only has a role to support as appropriate without taking total control.

3.5.4 The Board should establish mechanism / channel for the Board or management of the subsidiary to discuss and propose solution in case they disagree with direction of the parent or think business goals / direction lack efficiency, breach risk appetite, contradict with objectives, or not being for the utmost benefit of the subsidiary.

- 3.5.5 In case of associate company, the degree of authorization and participation (through representative director) in deciding strategy and operation targets of that associate company depend mainly on controlling power through sharer ownership, number of director / management sent into the associate company as well as details in the Shareholder Agreement (if any).

### 3.6 Authority scope of parent and subsidiaries / associate companies

- 3.6.1 The Board should clearly stipulate the chain of command and scope of authority between the parent and subsidiary, which could be divided into three levels as follow:

3.6.1.1 Items that the management of subsidiary can decide as deem appropriate.

3.6.1.2 Items that the Board of subsidiary can approve as deem appropriate.

3.6.1.3 Items that must be propose to the parent's Board and/or shareholders for approval.

The Board should also ensure that all items listed above are indicated in the subsidiary's "memorandum of association." In case of associate company (or subsidiary with other investors), the authority structure depends on the Shareholder Agreement as well as relevant laws, rules, and regulations.

- 3.6.2 The Board should clearly stipulate items that representative director is not entitled to use own discretion in casting vote and require prior approval from the parent's Board and/or shareholders (depend on the case) such as:

3.6.2.1 Director nomination

3.6.2.2 Annual / interim dividend payment (if any)

3.6.2.3 Significantly sell or transfer whole or part of the company to another person.

3.6.2.4 Buy or accept transfer of business of other company.

3.6.2.5 Merger

3.6.2.6 Termination of business

3.6.2.7 Borrow, lend, guarantee, oblige, or grant financial aid to other company that significantly affect the company's financial status.

3.6.2.8 Amend the company's articles of association.

3.6.2.9 Approve annual budget.

3.6.2.10 Capital raising, new share allocation, capital write-down, as well as other actions that could result in significant drop of the company's ownership.

3.6.2.11 Other cases prescribed by regulator's criteria or as deem appropriate.

Practically, companies usually stipulate that only strategic matters and significant issues of the company are required to get prior approval from the parent's Board and/or shareholders while they normally assign the Board of subsidiary / associate company to decide on operational matters.

- 3.6.3 Whenever subsidiary / associate company consider the aforementioned items, the parent's Board should arrange for Board meeting or shareholders' meeting (depend on the case) to consider the cases before the subsidiary holds Board meeting.
- 3.6.4 Even items that require approval from the parent's Board and/or shareholders, the Board may allow the Board of subsidiary / associated company to present their views or comments and use them as supporting information. Doing so will ensure the Board's decision is prudent and take into account benefits of all concerned parties.

### 3.7 Policy / guideline concerning key matters

- 3.7.1 In case the parent has full controlling power, the Board should set key policies for the subsidiary to be used as operating framework. It could be set as group-wide policy to ensure management direction alignment of both the parent and subsidiary. For instance,
- 3.7.1.1 Corporate Governance Policy / Code of Conduct
  - 3.7.1.2 Corporate Social Responsibility Policy
  - 3.7.1.3 Risk Management / Internal Control Policy
  - 3.7.1.4 Anti-Corruption / Whistleblowing Policy
  - 3.7.1.5 Conflict of Interest / Connected Transaction Policy
  - 3.7.1.6 Confidentiality and Insider Information Policy
  - 3.7.1.7 Other policies as deem appropriate
- 3.7.2 The Board should encourage the company to continuously communicate / distribute the policy and guideline to all subsidiaries, covering personnel of all levels. It may do so through standard training programs applicable to all companies in the group.
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- 3.7.3 Although group-wide policy could help aligning management directions of the parent and subsidiaries, but the Board should also aware that certain policy could be an obstacle, cause difficulty, or impractical with some subsidiaries due to different context and diverse environment. In such case, the Board should ensure the policy has adequate flexibility or allow the Board of subsidiary to stipulate policy / guideline by itself to match with specific conditions before proposing to the parent's Board for consent.
- 3.7.4 Practically, company may opt to have its Board approved only Group Philosophy and communicate with the Board of each subsidiary. The subsidiary's Board will then set up policy / guideline that matches its own context while the parent's Board only ensure the policy / guideline align and not contradict with the principle.
- 3.7.5 In case of associate company, the company may not have controlling power but it still can take part in the deciding key policy of the associate company (via representative director), depending on investment proportion and / or shareholder agreement (if any).

### 3.8 Effective communication and disclosure channels

- 3.8.1 Besides promoting positive relationship between the Board, management, and personnel within the group of companies, the Board should also set up clear "Communication policy / Parent-Subsidiary reporting policy" to ensure effective communication and mitigate risk of discorded operations.
- 3.8.2 The Board should arrange for "communication channel" that accommodate clear, transparent, and timely communication while providing "channel" for the Board to monitor and ensure that subsidiaries / associate companies effectively disclose information concerning their performances or significant items.
- 3.8.3 The Board should set policy requiring subsidiaries / associate companies to disclose key information (perhaps through representative director) to the parent such as
- 3.8.3.1 Monthly operating results, financial statements, and information supporting the financial statements for the parent to use in the preparation of its quarterly / annual financial statements.
  - 3.8.3.2 Report significant operating (or financial) issues to the parent upon detection or request.

- 3.8.4 Although the parent practically has controlling power and can access most information of subsidiary, the Board should ensure the company has a mechanism that allows minor shareholders (if any) to equally access such information.
- 3.8.5 In case both the company and subsidiary / associate company are listed companies, the Board should be extra careful with flows of information within the group of companies, potentially confidential information or insider information that could have material impact on stock price movement. (and has not yet been disclosed to the public) The Board should put in place prudent mechanism such as
- 3.8.5.1 Stipulate guideline to secure data in the information system.
  - 3.8.5.2 Assign right to access information to personnel at different levels.
  - 3.8.5.3 Signing of Confidentiality Agreement.
- 3.8.6 The Board may consider appropriate reporting framework for subsidiaries / associate companies to use as a guideline in preparing report for the parent. It may also stipulate reporting frequency and key items expected to be reported by subsidiaries / associate companies. (See Annex 4)

### 3.9 Corporate control / audit mechanism

- 3.9.1 The Board should ensure subsidiaries / associate companies have appropriate and prudent internal control, internal audit, compliance, risk management systems. It should have a role as reviewer to ensure the Boards of subsidiaries / associate companies are accountable for putting in place such systems and that they function effectively.
- 3.9.2 In case the subsidiary / associate company is a listed company (or financial institution), "Audit Committee" and / or "Risk Management Committee" of the subsidiary / associate company is responsible to audit and evaluate the effectiveness of such systems. Some group of companies may stipulate additional guideline for Audit Committees of subsidiaries / associate companies to meet with Audit Committee of the parent at least once a year to exchange views and discuss key issues or challenges facing them.
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- 3.9.3 In case the subsidiaries / associate companies are small and not listed, the aforementioned units may be “centralized” or share resources with the parent. (or other company with controlling power) For instance, a policy could be stipulated that
- 3.9.3.1 Audit Committee of the parent has roles and responsibilities in auditing and evaluate the effectiveness of internal control, risk management, compliance, and corporate governance systems of subsidiaries.
  - 3.9.3.2 Internal audit unit of the parent is authorized to gain direct access to information, system, and personnel of subsidiaries as necessary and appropriate. It should audit subsidiaries at least once a year and report the results to the parent’s Audit Committee.
  - 3.9.3.3 The management of subsidiaries have duties to coordinate and facilitate a visit by the parent’s Audit Committee to query and make observation about operations of the subsidiaries at least once a year.
- 3.9.4 The Board should weigh evaluation result of internal control and risk management systems of each subsidiary / associate company in considering or reviewing issues such as
- 3.9.4.1 Key risks of subsidiary / associate company as well as likelihood and impact. (on the parent and the subsidiary / associate company)
  - 3.9.4.2 Ranking risks and appropriate risk mitigation / risk management methods.
  - 3.9.4.3 Risk appetite of the subsidiary / associate company.
  - 3.9.4.4 Risk management policy that aligns with risk appetite.
- 3.9.5 The Board should be aware that certain systems such as risk management and compliance may require help from personnel with in-depth view of the subsidiary at operational level. (which may be because the subsidiary is not in the same industry as the parent or operate business under specific legislations) Therefore, centralizing these systems or sharing all resources with the parent without sufficient collaboration with personnel of the subsidiary could make these mechanisms ineffective.

- 3.9.6 In case the company has numerous subsidiaries under it or has complex group structure, the Board may consider allowing each subsidiary to set up separate “internal audit unit,” “compliance unit,” and “risk management unit” on its own. These units must report significant information as well as performance result to the management / Board of the subsidiary for initial review before forwarding to the Board, Audit Committee, or relevant committees of the parent for consideration to demonstrate overall internal control mechanism of the group.
- 3.9.7 Subsidiary should have “whistleblowing channel” for anyone detecting malpractice or untransparent actions. The Board or CEO of the subsidiary may consider appointing “Investigation Committee” to probe the complaint as appropriate. The Board may stipulate that at least one member of the Investigation Committee come from a unit of the parent. (such as internal audit unit)

### **3.10 Items with potential conflict of interest**

- 3.10.1 The Board should establish a mechanism to prevent “conflict of interest” that may result from any action of director or management of subsidiary / associate company or when engaging in connected transaction between the parent, subsidiary, and associate company.
- 3.10.2 In case of intra-group transaction (such as lending, granting guarantee, purchasing goods) which may trigger conflict of interest, the Board should ensure the company complies with “connected transaction policy” as well as approval criteria and procedures on arms’ length basis by emphasizing the utmost benefit of the company.
- 3.10.3 The Board should stipulate explicit “prohibition” for any action or transaction that clearly consider or trigger conflict of interest with the company such as
- 3.10.3.1 The Board and management of subsidiary / associate company as well as relevant persons must not use insider information of the company and subsidiary / associate company obtained from performing duties or any other way for to benefit oneself or others either directly or indirectly.
- 3.10.3.2 The Board and management of subsidiary / associate company must not attend meeting or cast vote on issues they have interests in.
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3.10.3.3 The Board and management of subsidiary / associate company must not buy or sell securities of the company within one month prior to the announcement of quarterly financial statement and one day after the announcement.

3.10.3.4 Other prohibition as deem appropriate.

3.10.4 The Board should ensure compliance with such policy / regulations and that the company discloses connected transaction accurately and completely in annual registration statement and annual report.



# Annex

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## Annex 1 Subsidiary, associate company, and relevant definitions

Definition of terms about governing subsidiaries / associate companies could be elaborated and interpreted in various ways, depending on units authorized to provide the definition, objectives for usage of these terms, and other relevant context.

However, terms in this guideline mainly adhere to meanings that align with “definition” of the terms stipulated in the Securities and Exchange Commission Announcement at K.J. 17/2551 Re: Defining terms in announcement about issuing and offering securities (Compilation) that compiled amendments up to the fourth amendment. (effective from July 16, 2012)

1 The Board should have adequate comprehension in definition of the following terms:

1.1 **Major company** or “parent” (as appeared in this guideline) refers to any company that have direct or indirect “controlling power” over the other company.

1.2 **Controlling power** refers to power to determine financial policy and operations of the company to gain benefits of that company. Such power occurs upon one of the following conditions:

1.2.1 Your company owns more than 50% of shares with voting rights in that company.

1.2.2 Your company has power to control majority votes at shareholders’ meeting of that company, either directly or indirectly. For examples, your company may have power to control over half of voting rights due to agreement made with other shareholders or that your company has legal rights.

1.2.3 Your company has controlling power to appoint or dismiss at least half or all the Board of that company, either directly or indirectly.

1.3 **Subsidiary** refers to company that falls into any of the following conditions:

1.3.1 Any company that your company has controlling power or

1.3.2 Any company the company (under 1.3.1) has controlling power or

1.3.3 Any company under successive controlling power, starting from the company (under 1.3.2)

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1.4 **Associate company** refers to company that falls into any of the following conditions:

- 1.4.1 Any company that your company (or your subsidiary) owns combine stake of at least 20% but not exceeding 50% of total voting rights of that company.
- 1.4.2 Any company that your company (or your subsidiary) has power to take part in deciding financial policy and operations of the company but not to the extent that can control the policy and not considered to be subsidiary or joint venture.

#### Case study

##### Fact

- Company A owns 80% stake in Company B
- Company B owns 90% stake in Company C

##### Therefore,

- Company B is subsidiary of Company A (Under definition in 1.3.1)
- Company C is subsidiary of Company B (Under definition in 1.3.1)
- Company C is subsidiary of Company A (Under definition in 1.3.2)

2. Subsidiary may operate similar or different business than the parent. It could be a new company set up directly by the parent's funding (or with other investors) or it could derive from acquisition of other existing company by the parent through equity accumulation until it gains controlling power.
3. Parent may have one of the following business characteristics:
- 3.1 Pure Holding Company or Non-Operating Holding Company is a company that does not operate significant business by itself while revenues derive mainly from holding stakes in subsidiaries. This type of parent usually has objective "to control" rather than "to invest."
- 3.2 Mixed Holding Company or Holding-Operating Company is a parent company that operates core business by itself such as manufacture, distribute, offer services, trade along with investment in subsidiaries to seek general return.

4. Parent, subsidiary, and associate company are considered separate legal entities which create two legal effects including
    - 4.1 Subsidiary / associate company has a status as separate juristic person than the company that hold shares.
    - 4.2 Company that hold shares has limited civil liability equal to the amount of unpaid shares as if there is corporate veil that protect liability on the company.
  5. Company may invest in many subsidiaries / associated companies and these companies may hold shares in each other. (cross holding) This type of structure is commonly called Corporate Group.
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## Annex 2 Observation points for the Board concerning parent–subsidiary relationships

		Subsidiary	
		Highly dependent on the parent	Less dependent on the parent
Parent	Highly dependent on the subsidiary	<p><b><u>Mutual Dependence</u></b></p> <ul style="list-style-type: none"> <li>How can the company assess pricing rationality in connected transaction between parent and subsidiary given no market price that can be used as reference?</li> <li>Is it possible that the subsidiary sees no necessity to develop its products because it operates in close system with no competition?</li> <li>Does the company need to initiate appropriate incentive for the subsidiary to promote development or innovation (which will benefit the subsidiary itself) and how?</li> <li>How does the company plan to manage knowledge within the Corporate Group to catch up with external knowledge and enhance competitiveness of the subsidiary?</li> <li>As both sides are highly dependent on each other, is it necessary to stipulate that controlling and decision-making authorities depend directly on the parent?</li> <li>Other issues in accordance with context of each company.</li> </ul>	<p><b><u>Dual-Focused</u></b></p> <ul style="list-style-type: none"> <li>Is it possible that the subsidiary be pressured to engage mainly in transactions with the parent until it triggers conflict of interest and causes the subsidiary to lose business opportunity?</li> <li>What are control / probe measures can the company use to prevent such conflict of interest?</li> <li>How necessary it is to have agreement between parent and subsidiary on resources allocation (for the parent / other clients) to create utmost benefit for the Corporate Group.?</li> <li>Other issues in accordance with context of each company.</li> </ul>
	Less dependent on the subsidiary	<p><b><u>Unilateral Dependence</u></b></p> <ul style="list-style-type: none"> <li>Is it possible that the subsidiary may overdependent on revenues within the Corporate Group (especially from the parent) until it lacks bargaining power or see no necessity to develop its products?</li> <li>What is the direction in developing competitiveness of the subsidiary to match industry peers and build up bargaining power?</li> <li>Does the company need to explore ways to drive / promote the subsidiary to access new customer segments to mitigate risk of overdependent on the parent and how?</li> <li>Other issues in accordance with context of each company.</li> </ul>	<p><b><u>Independence</u></b></p> <ul style="list-style-type: none"> <li>Since the parent may not have as much experience and expertise as the subsidiary in the latter's business, will it be appropriate for the parent to have total strategic control or should it restrict the roles to ensure operating results align with the framework?</li> <li>In case of decentralized governance, what is the appropriate authority scope of the subsidiary and should there be delegation contingent upon performance?</li> <li>Is it necessary for the parent to take part in the decision-making, especially on significant strategic issues, even when using decentralized governance model?</li> <li>Is it possible for the parent (and other subsidiary under it) to cooperate with the subsidiary with an aim to create synergy as well as enhance competitiveness and overall productivity for growth of the Corporate Group?</li> <li>Other issues in accordance with context of each company.</li> </ul>

### Annex 3 Initial checklist for the Board in governing subsidiary

Initial checklist for the Board in governing subsidiary			
No.	Details	Yes	No
1	Does the company have clear process / guideline about managing subsidiary investment (covering full life cycle from establishment to termination)?		
2	Has the company laid CG framework for subsidiaries with balanced emphasis on both compliance and performance aspects?		
3	Has the company arranged for the establishment of subsidiary board, comprising persons with appropriate qualifications, knowledges, and competencies that are useful for business operations of the subsidiary?		
4	Does the size, structure, and composition of the subsidiary's Board consider appropriate and meet relevant requirements (such as proportionate to shareholding)?		
5	Has the company set clear delegation of authority for the Boards of subsidiary and parent as well as shareholders?		
6	Does the company allow subsidiary to provide suggestions or useful information to be used for reviewing strategy / operating goals of the Corporate Group.		
7	Has the company set group-wide policy to steer operations of the parent and subsidiaries into the same direction / standard.		
8	Has the company provided subsidiary appropriate flexibility in adjusting policies in accordance with business context, environment, as well as relevant rules, regulations, and laws of the country that the subsidiary operates in?		
9	Has the company arranged for appropriate communication and disclosure channels as well as chain of command between parent and subsidiary?		
10	Has the company arranged for the subsidiary to have appropriate and adequate internal control, risk management, and compliance mechanisms?		
11	Has the company arranged a mechanism or channel for the parent's Board to continuously monitor and evaluate the subsidiary's performance?		

**Remark:** The Board may apply this Checklist in governing associate company and/or any other company that the company has invested significantly in accordance with the context and as appropriate.

## Annex 4 Example of reporting format/framework for subsidiary to propose to parent's Board

Reporting topics	Reporting frequency		
	Upon occurrence	Quarterly	Annually
<b>Performance of subsidiary</b>			
• Business situation / Industry trend		✓	
• Competition strategy		✓	
• Business opportunities / threats and ways to manage		✓	
• Other significant issues		✓	
<b>Significant items or transactions such as</b>			
• Director nomination at subsidiary	✓		
• Dividend payment of subsidiary	✓		
• Significantly sell or transfer whole or part of subsidiary.	✓		
• Buy or accept transfer of other company into subsidiary.	✓		
• Merger of subsidiary	✓		
• Termination of subsidiary	✓		
• Borrow, lend, guarantee, oblige, or grant financial aid to other company that significantly affects subsidiary's financial status.	✓		
• Amend the subsidiary's articles of association.	✓		
• Capital raising, new share allocation, capital write-down of the subsidiary (directly and indirectly) that could result in significant change of parent's ownership.	✓		
<b>Financial Reports</b>			
• Balance sheet			✓
• Statements of cashflows			✓
• Other financial information necessary for preparation of notes to financial statements.		✓	
"Connected transaction" under criteria of regulator.	✓		

**Remark:** The Board may apply this Checklist in governing associate company and/or any other company that the company has invested significantly in accordance with the context and as appropriate.

## Annex 5 Example Key issues for evaluation of Board efficiency and readiness to perform duties

Key issues for the Board of subsidiaries / associate companies		Evaluation result			
		1	2	3	4
1	You have in-depth understanding of the reasons or objectives that make the parent decide to invest in the subsidiary / associate company.				
2	You have concrete knowledge of the “parent’s expectations” toward your roles as director of the subsidiary / associate company.				
3	You have clear written “Board charter of the subsidiary / associate company” to be used as reference in performing your duties.				
4	You have concrete knowledge of issues that you can use “discretion” because the level of authority has been clearly agreed upon.				
5	You know exactly “when” you must present information or report issues to the parent’s Board.				
6	You are of view that Board of the subsidiary / associate company that you are a member of comprising persons with appropriate qualifications, knowledge, and competencies for the business.				
7	You are of view that the Board can effectively govern subsidiary / associate company in alignment with the parent’s strategy and risk appetite.				
8	You have adequate understanding about business relationships and level of dependence between the parent, your company, and other subsidiaries / associate companies within the Corporate Group.				
9	You have adequate understanding about legal issues or conditions / regulations of subsidiary / associate company that are different than the parent.				
10	As director of subsidiary / associate company, you have constantly delivered key information or useful comments for the parent to review strategy.				
11	You are of view that policy / guideline about business operations assigned by the parent has sufficient flexibility and align with context of the subsidiary / associate company.				
12	Although using the parent’s policy as a base for decision-making, you will ensure the decision also take into account utmost benefits of other investors. (if any)				
13	You have a mechanism to meet or seek professional advice from the parent’s Board immediately should there need decision on issues that interests of parent do not align with subsidiary / associate company.				
14	You have performed your duties with prudent information confidentiality (of both the parent and subsidiary) in accordance with rules/ regulations of the regulator.				
<b>Evaluation criteria: (1) Strongly disagree (2) Disagree (3) Agree (4) Strongly agree</b>					

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