



**RESERVE BANK OF MALAWI**

# **CORPORATE GOVERNANCE GUIDELINES**

**April 2010**

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## **Authority**

1. These Guidelines are issued pursuant to Sections 26 and 57 of the Banking Act, 1989. The Guidelines may be cited as Corporate Governance Guidelines and shall apply to all entities licensed under the Banking Act, 1989 in Malawi.
2. While the Banking Act, 1989 authorizes the RBM to issue directives, guidelines have been issued in lieu of a directive.

## 1.0 INTRODUCTION

Corporate governance<sup>1</sup> is the process and structure used to direct and manage the business and affairs of an institution with the objective of ensuring its safety and soundness and enhancing shareholder value. The broad nature of corporate governance has led to a tendency to consider it as a concept rather than emphasizing the definition. It encompasses appropriate management and control structures of an entity. Further, it includes rules relating to power relations between owners, the board, management and other stakeholders. For banks, the process and structure define the division of power and establish mechanisms for achieving accountability between the board of directors, management and shareholders, while protecting the interests of depositors and taking into account the effects of such processes on other stakeholders, such as creditors, employees, customers and the general community.

Banks and financial institutions occupy a special position of trust in the national economy and their corporate governance is therefore, a matter of paramount importance. They provide basic financial services to the public, financing to commercial enterprises and access to the payment system. By nature, banks are highly leveraged, with most of their funds coming from depositors and creditors. Increasing globalization of financial markets, emergence of conglomerate structures, technological advances and innovations in financial products have added to the complexity of risk management in the financial sector. Explicitly, there are several structural reasons explaining why corporate governance has become more important and of first order for economic development and well being. The private, market-based investment process is now much more important for most economies than it used to be. With size of firms increasing and the role of financial intermediaries and institutional investors growing, decisions about mobilizing capital are now one step removed from the principal owner. At the same time, the opening up and liberalization of financial and real markets have broadened investment choices and made decisions about allocation of capital and stewardship more complex, while structural reforms, price deregulation and increased competition, have increased corporate exposure to risk from multiple forces. For these reasons the quality of corporate governance expected of banks is high, as capital can no longer guarantee operational existence. Recent corporate scandals give empirical evidence of the need and

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<sup>1</sup>Sir Adrian Cadbury in the Report on Financial Aspects of Corporate Governance, 1992, defines corporate governance as 'the system by which companies are directed or controlled'. Here corporate governance is defined as a set of mechanism through which firms operate when ownership is separated from management. However, most codes of best practice deal with corporate governance as a concept and explain its importance without defining its meaning. Whatever the approach is chosen, it is important that fundamental values of transparency, accountability,

importance of corporate governance.

Additionally, these institutions operate within an ever-changing framework of laws and are subject to direct control of the board of directors. The board must ensure that the law is adhered to while simultaneously ensuring that strategies for long-term success are set and implemented. It is, therefore, necessary to achieve a balance and alignment among external and internal controls, risk management and competitive behaviour while at the same time operate within the principles of good corporate governance outlined in these Guidelines which include: discipline, transparency, independence, accountability, responsibility, fairness and social responsibility.

These Guidelines set forth a broad framework of fundamental corporate governance principles to guide the actions of the directors and managers of the commercial banks operating in Malawi.

## **2.0 PURPOSE OF CORPORATE GOVERNANCE IN THE SUPERVISORY PROCESS**

The boards of directors and senior management of the banks play key control functions in the Reserve Bank of Malawi's (RBM) supervisory framework. Effective oversight by directors and senior management is an essential element in the safe and sound functioning of banks. Effective oversight is also essential for the maintenance of an efficient and cost-effective supervisory system. Effective oversight helps protect depositors and allows the RBM to rely on the bank's internal processes, thereby reducing the amount of resources required for the RBM to meet its supervisory mandate. In addition, in situations where an institution is experiencing problems, or where significant corrective action is necessary, the important role of the board is heightened and the RBM requires momentous board involvement in seeking solutions and in overseeing the implementation of corrective actions.

The RBM supervises licensed institutions to assess their condition and monitor their compliance with applicable laws. This is carried out through both on site and off site supervision. The RBM rates banks using both the CAMELS scale and Risk Matrix, key among it is the consideration of quality of oversight and control provided by the board of directors and management.

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fairness and responsibility be respected in order for firms to build and sustain the confidence of investors, stakeholders and society as a whole.

### 3.0 **DEFINITIONS**

In these Guidelines, unless the context otherwise requires –

*'affiliate'* means a company or enterprise that controls or is under common control with a bank. For purposes of this definition, “control” means the ability to exercise dominant influence over the management or the policies of the company and can be exercised through ownership ability to exercise voting rights or ability to control the election of majority board members.

*'bank'* shall have the same meaning as ascribed in the Banking Act.

*'board'* (board of directors) of a bank means the highest body of authority in a licensed institution responsible for strategically guiding the licensed institution, effectively monitoring management, and properly accounting to shareholders.

*'executive officer'* means an officer at the most senior level of management of the licensed institution (whether or not he/she is director) who effectively manages that licensed institution.

*'executive director'* means a member of the board of directors who is involved in the day-to-day management of an institution and/or is in full time salaried employment of the institution or any of its subsidiaries or affiliates .

*'independent non-executive director'* means a person that either:

- i. is nominated by the other directors or executive management of the institution
- ii. is not related or affiliated to a shareholder that has the ability to control or influence management; or
- iii. has not been employed by the institution or its subsidiary in any executive capacity for the preceding three financial years; or
- iv. is not a member of the immediate family of an individual who is or has been in any of the

past three financial years employed by the institution or the group in an executive capacity; or

- v. is not a professional advisor to the institution or the group other than in a director capacity; or
- vi. is not a significant customer or supplier of the institution; or
- vii. has no significant contractual relationship with the institution or group; or
- viii. is free from any business or other relationship which could be seen to materially interfere with the individual's capacity to act in an independent manner.

*'insider'* shall have the same meaning as ascribed in the Directive on Transactions with Related Persons.

*'internal control'* shall mean a process effected by the institution's board of directors, management and other personnel designated to provide reasonable assurance regarding the achievement of objectives such as effectiveness and efficiency of operations, reliability of financial reporting and compliance with applicable laws and regulations.

*'internal audit'* means an independent, objective assurance and consulting activity designed to add value and improve an organization's operations and which helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

*'non-executive director'* means a person not involved in the day-to-day management and not a full time salaried employee of the institution or any of its subsidiaries and affiliates and sits on the board.

*'related party'* shall have the same meaning as ascribed in the Directive on Transactions with Related Persons.

*'senior management official'* shall have the same meaning as ascribed in the Directive on New Directors, Audit Committee Members and Senior Management Officials.

'stakeholder' means an individual or group, in addition to shareholders, who have an interest in, and/or influence over, the institution's operations and the achievement of the institution's goals, such as creditors, employees, suppliers, customers and the community.

## **APPLICATION OF THESE GUIDELINES**

### **4.0 SHAREHOLDERS**

#### **Principle I**

*Shareholders of banks shall jointly and severally protect, preserve and actively exercise their supreme authority over the institution in annual general meetings (AGM). They shall foster constructive relationships with their respective boards that encourage them to engage constructively with the respective entities.*

#### **Guidelines**

- 4.1 Shareholders shall ensure that the board have clear policies for shareholder relations and at least annually review practices, aimed at clearly communicating the goals, strategies and achievements of the institution.
- 4.2 Shareholders shall when deemed necessary, question external auditors on the auditors' opinion during the annual general meeting or extraordinary meetings.
- 4.3 Shareholders shall ensure that only competent and reliable persons who can enrich and add value to the institution are elected or appointed to the board of directors.
- 4.4 Shareholders shall ensure that the board is constantly held accountable and responsible for the efficient and effective governance of the institution.
- 4.5 Shareholders shall change the composition of a board that does not perform to expectation or in accordance with the mandate of the institution.
- 4.6 No shareholder with more than 10 percent (10%) shareholding in a banking institution shall be an executive director or form part of the management of the institution.

4.7 Shareholders shall fix and approve director's remuneration/fess during annual general meetings or extraordinary meetings.

## 5.0 **BOARD RESPONSIBILITIES AND COMPOSITION**

### **Principle II**

*The board of directors' role is to oversee the proper functioning of the institution. In order to achieve this, the board shall have clear, well- defined and understood responsibilities. There shall be a balance of skills, knowledge, experience and perspectives among directors so that the board works effectively to ensure the long-term safety and soundness of the institution.*

### **Guidelines**

5.1 The board shall:

5.1.1 Have a formal charter that sets out its responsibilities, which shall be disclosed in summary in the annual report. A charter shall, at a minimum, confirm the board's responsibility for the formulation and adoption of strategic plans, the monitoring of operational performance and management. The charter shall allow the board to determine appropriate policies and processes to ensure the integrity of the institution's risk management practices and internal controls, communications policy, and director selection, orientation and evaluation;

5.1.2 Retain full and effective control over the institution and be responsible for monitoring management in respect of implementation of the board's plans and strategies;

5.1.3 Give strategic direction to the institution, discuss and approve the organisational structure of the institution. The Board should appoint and remove the management of the institution; and ensure that succession is planned throughout the organisation;

5.1.4 Allocate time and resources for directors to acquire and retain a sound understanding of

their responsibilities and this shall include an orientation program to ensure that incoming directors are familiar with the institution's business and governance practices. It is equally important that directors should receive further relevant training, particularly on relevant new laws, regulations and changing commercial risks from time to time;

- 5.1.5 Have rigorous formal processes for evaluating its performance along with that of board committees and individual directors;
- 5.1.6 Ensure that the institution complies with all relevant laws, and codes of business practice, and that it communicates with its shareholders and relevant stakeholders openly and promptly;
- 5.1.7 Ensure that management maintains an effective compliance function that routinely monitors adherence to rules, regulations and policies to which the institution is subject and ensures that any deviations are reported to an appropriate level of management or, if necessary, the board;
- 5.1.8 Have access to all the institution's information, records, documents and property;
- 5.1.9 Have an agreed procedure, and access to budget resources, to enable directors, if necessary, to obtain independent professional advice at the institution's expense;
- 5.1.10 Identify and monitor the non-financial aspects relevant to the business of the institution including reputation risk;
- 5.1.11 Ensure that senior management implements policies to identify, prevent or manage and disclose as appropriate the conflicts of interest which may arise as a result of its affiliation or transactions with affiliated entities; and
- 5.1.12 Ensure that the institution maintains a positive image within the industry and the economy as a whole. To this extent, therefore, the institution is expected to provide

adequate services and facilities both efficiently and competitively in line with safe and sound banking practices.

5.2 An institution's board shall have a majority of non-executive directors and shall include directors who meet the criterion of 'independent non-executive' directors so as to safeguard all the stakeholders' interests.

5.2.1 The chairperson of every institution shall be a non-executive director. No director of an institution shall simultaneously hold the roles of board chairperson and chief executive (or equivalent) for the same institution;

5.2.2. The chairperson shall be responsible for fostering a constructive governance culture and applying appropriate governance principles among the directors and with management;

5.2.3 Procedures for appointments to the board shall be formal and transparent, and be a matter for the board as a whole, assisted by a nominations committee. Selection and appointment of directors, a majority of whom shall be non- executive and resident in Malawi, shall be through formal processes designed to give the board a range of relevant skills, expertise and experience;

5.2.4 The Board should comprise directors who as a group provide core competencies such as accounting or finance, business or management experience, industry knowledge, strategic planning experience or knowledge;

5.2.5 There shall be an appropriate balance of power and authority on the board, such that no one individual or group of individuals shall dominate the board's decision making process;

5.2.6 The nominations committee shall constitute only non-executive directors, of whom the majority shall be independent;

- 5.2.7 The nominations committee shall ascertain whether potential new directors are suitable for the position in terms of the *fit and proper test*, requirements of the Banking Act and the directive on new directors, audit committee members and senior management officials;
- 5.2.8 Board continuity, subject to performance and eligibility for re-election, is imperative, and a programme ensuring a staggered replacement of directors shall be put in place;
- 5.2.9 The annual report of banks shall include information on the name, age, experience, education, affiliation, and committee membership of each director. The reports should also identify which directors are independent, and include the respective dates of the board members' appointments and their percentage shareholding in the institution and other companies if applicable;
- 5.2.10 To avoid conflict of interest with their existing audit clients, practicing accountants of audit firms that audit the institution shall not be appointed as directors of that institution;
- 5.2.11 Every director shall make all efforts to attend all board meetings of the institution. The duty of care requires that a director discharges his or her duties and responsibilities effectively. At its annual general meeting, each institution shall be required to review the suitability of every director who has failed to attend at least 75% of board meetings. Attendances shall be disclosed in the annual report; should the AGM reappoint a director who was absent for at least 75% of the board meetings, the director shall cease to be a member of the board if he fails to attend 50% of the meetings in the subsequent year(s).
- 5.2.12 A director of the bank shall not be a member of more than six other boards. In this clause, 'board' means board of a corporate entity or company incorporated under the Companies Act, 1984.
- 5.2.13 A director shall not be a member of more than one institution licensed under the Banking Act, 1989 unless the said institution is a subsidiary or holding company of the financial institution;

5.2.14 Independent non-executive directors shall not be considered independent after serving on the board for a period of more than ten (10) years; and

5.2.15 The Board shall report to the Reserve Bank of Malawi the resignation and/or removal of any of its members within seven days.

## **6.0 BOARD COMMITTEES**

### **Principle III**

*The board shall use committees where this would enhance its effectiveness in key areas while retaining its overall responsibility. Board committees assist the board of directors in discharging its duties and responsibilities more effectively and efficiently.*

*Committees should preferably be made up of non-executive directors. The inclusion of management on these committees shall be an exception rather than the rule, to reinforce the independence of the board. Management may, however, be invited to provide input on any matter that is of interest to the board.*

### **Guidelines**

- 6.1 At a minimum each board shall ensure the following committees are in place: Audit Committee, Risk Management Committee, and Credit Review Committee. In addition, each board shall endeavor to have the Nominations (Appointments) and Remuneration Committee.
- 6.2 Every board committee shall have a clear, formal charter that sets out its role, schedule of meetings and delegated responsibilities whilst safeguarding the ultimate decision making authority of the board as a whole.
- 6.3 The summary of the charter and membership of each board committee shall be published in the annual report.
- 6.4 Proceedings of committee meetings shall be properly minuted and reported back to the board to allow the other directors to be informed and seek clarification from the

committee members if so desired.

- 6.5 All board committees shall preferably be chaired by a non- executive director. The board chairman should not be a member of any subcommittee. The board should strive to eliminate dual membership of oversight committees of the board such as audit committee and risk taking sub committees like credit risk committee.
- 6.6 All board committees shall be free to take independent, external professional advice as and when deemed necessary at the institution's cost.
- 6.7 All board committees shall be subjected to regular evaluation by the board to ascertain their performance and effectiveness. Board committee charters shall be reviewed regularly and modified when necessary.
- 6.8 The board shall consider occasional rotation of members and the chairperson of all board committees taking into account the specific experience and knowledge required to sit on a particular committee.
- 6.9 The Chief Executive Officer shall not be a member of board audit sub-committee.

## **7.0 EVALUATION OF BOARD PERFORMANCE**

### **Principle IV**

*Self-evaluation is a proactive, best practice by boards that intend to excel to higher levels of performance. The review seeks to identify specific areas in need of improvement or strengthening. The results and any actions to be taken shall be discussed by the full board.*

### **Guidelines**

- 7.1 The board, through its nominations committee, shall review its required mix of skills and experience and other qualities such as diversity in order to assess its effectiveness. Such review shall be by means of peer and self-evaluation of the board as a whole, its committees and the contribution of each and every director including the chairperson.
- 7.2 Individual evaluation should aim to assess whether each director continues to contribute effectively and demonstrate commitment to the role (including commitment of time for board and committee meetings and any other duties). The Chairperson should act on the results of the self-evaluation, and where appropriate, propose that new members be appointed to the Board or

seek resignation of directors, in consultation with the Nomination Committee.

- 7.3 The evaluation shall be conducted annually, and every institution shall be required to disclose in the annual report that this has been done. The report on the board and directors' effectiveness shall be submitted to the RBM on request. Board evaluation shall be based on the guidance provided in Appendix 1 of these Guidelines.
- 7.4 The review and evaluation shall include, among other things, an assessment of the board's:
- 7.4.1 Composition and independence;
  - 7.4.2 Performance against its objectives at the beginning of the year;
  - 7.4.3 Performance against the board charter;
  - 7.4.4 Effectiveness in the institution's strategic direction;
  - 7.4.5 Response to problems and crises;
  - 7.4.6 Responsiveness to shareholders' and stakeholders' concerns;
  - 7.4.7 Maintenance and implementation of the board's governance principles;
  - 7.4.8 Access to and review of information from management and the quality of such information; and
  - 7.4.9 Opinion on coercion or influence from a dominant entity be it shareholder, other director or management that affects delivery on the board.

## **8.0 ROLES OF SENIOR MANAGEMENT**

### **Principle V**

*It is the responsibility of management, under the direction of the chief executive officer, to conduct the institution's business and affairs in an effective, responsible and ethical manner, consistent with the principles and direction established by the board through the strategic plan.*

### **Guidelines**

#### **8.1 Board Chairman**

The Chairman shall:

- 8.1.1 Run the board and set its agenda. The agenda should take full account of the issues and concerns of all board members. Agendas should be forward looking and concentrate on strategic matters.
- 8.1.2 Ensure that the members of the board receive accurate, timely and clear information, in particular about the institution's performance to enable the board to take sound decisions, monitor effectively and provide advice to promote the success of the company.
- 8.1.3 Ensure effective communication with shareholders and ensure that members of the board develop an understanding of the views of the major shareholders.
- 8.1.4 Manage the board to ensure that sufficient time is allowed for discussion of complex or contentious issues, where appropriate arranging for informal meetings beforehand to enable thorough preparation of for the board discussion.
- 8.1.5 Take the lead in providing a properly constructed induction programme for new directors that is comprehensive, formal and tailored, facilitated by the Company Secretary.
- 8.1.6 Ensure that the performance of individuals and of the board as a whole and its committees is evaluated at least once a year.
- 8.1.7 Encourage active engagement by all members of the board.

## **8.2 Senior Management**

- 8.2.1 Senior management shall have the necessary skills to manage the business under their oversight and have appropriate control over key individuals in these areas;
- 8.2.2 Senior management shall implement strategies and policies approved by the board;
- 8.2.3 Senior management shall ensure that strategies and policies are communicated to all relevant staff;
- 8.2.4 Senior management shall ensure adequate segregation of duties and adherence to the four eyes principle<sup>2</sup> on key decisions committing the bank;
- 8.2.5 Senior management should provide the board with timely, relevant, and complete reports on the implementation of business strategy; and

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<sup>2</sup> A requirement or arrangement where execution of a transaction significantly committing the banking institution, has to be done only after two authorized officers (at least) are agreeable to the transaction.

- 8.2.6 Senior management should be held liable for false or misleading statements to the board, staff, market and regulators.

### **8.3 Chief Executive Officer**

- 8.3.1 The chief executive officer and the chairman of the board shall be separate persons, to ensure an appropriate balance of power, increased accountability and greater capacity of the board for independent decision making. In addition, institutions should disclose the relationship between the Chairperson and Chief Executive Officer where they are related to each other;
- 8.3.2 The chief executive officer shall be a suitably qualified person with appropriate and relevant experience and shall possess a proven track record at senior management level;
- 8.3.3 The chief executive officer shall be subjected to a fit and proper test and vetting by RBM in line with the requirements of the Banking Act and Directive on Appointment of Senior Management Officials prior to taking up appointment in the bank;
- 8.3.4 The chief executive officer shall be directly responsible for the day-to-day operations of the institution. The chief executive officer shall be conversant with the operations of the institution, state of internal controls, requirements of legislation, as well as current issues and policies affecting the financial sector;
- 8.3.5 Where the chief executive officer is absent for more than 21 days, an institution shall be required to notify and provide the RBM with details of the person appointed to act in that position. The person so nominated shall be fully acquainted with the affairs of the institution and shall be able to act promptly and with authority, on matters affecting the institution; and
- 8.3.6 An institution shall not make any public announcement about any proposed appointment of the chief executive officer or director before it obtains the RBM's written consent for the proposed change.

### **8.4 Company Secretary**

- 8.4.1 The company secretary of an institution shall be a lawyer, Chartered accountant or Chartered secretary or a firm or any person of similar capabilities that the RBM deems fit. The role of a Company Secretary and Chief Executive Officer shall be

separated.

- 8.4.2 The company secretary shall be duly empowered by the board to enable the company secretary to fulfill the prescribed duties;
- 8.4.3 The company secretary shall provide the board as a whole and directors individually with detailed guidance as to how their responsibilities shall be properly discharged in the best interest of the institution and in compliance with laws, internal rules and corporate governance guidelines;
- 8.4.4 The company secretary shall be responsible for the induction and continuing training of directors, and for assisting the chairperson and the chief executive officer in determining the annual board plan and the administration of other issues of a strategic nature at board level. Copies of the induction and continuing training programme shall be made available to the RBM on request;
- 8.4.5 The company secretary shall be a central source of guidance and advice to the board, and to the institution in general on matters of ethics and good governance; and
- 8.4.6 The company secretary shall be subjected to a fit and proper test by the RBM in the same manner as is recommended for all new director appointments.

## **8.5 Chief Financial Officer**

- 8.5.1 The chief financial officer, in addition to the requisite academic and professional qualification, shall be of good standing;
- 8.5.2 The chief financial officer shall be subjected to a fit and proper test by the RBM.
- 8.5.3 The chief financial officer should be a member of the local accountancy body (SOCAM).
- 9.4.4 The Chief Financial Officer shall furnish necessary and classified information to the board together with an analysis and suggestions as may be necessary. Among the key information to be prepared and presented before the board shall include: annual budgets, cash flow projections, forecast and long term plans; capital budgets and overhead budgets along with variance analyses; and quarterly operating results of the institution.
- 8.5.4 The Chief Financial Officer shall provide all necessary data presented in the 'Director's Report' to the shareholders. For this purpose, he/she must ensure that: financial statements present fairly the institution's state of affairs, the results of its operations, cash

flows and changes in equity; information; proper books of accounts of the institution have been maintained; appropriate accounting policies have been consistently applied in preparation of financial statements and that accounting estimates are based on reasonable and prudent judgement; and the system of internal is sound in design and has been effectively implemented and monitored.

8.5.6 The Chief Financial Officer shall be responsible for internal and external reporting of all financial information of the institution.

## **9.0 ETHICAL STANDARDS & CORPORATE VALUES**

### **Principle VI**

*The board of directors, in keeping with their responsibilities to the shareholders and other stakeholders, is committed to the achievement of business success and the enhancement of long-term shareholder value with the highest standards of integrity and ethics. Each director, as well as each member of senior management, is therefore expected to lead by example in a culture that emphasizes trust, integrity, honesty, judgment, respect, responsibility and accountability.*

### **Guidelines**

9.1 The board shall ensure that senior management implements strategic policies and procedures that are designed to promote good and acceptable ethical behaviour.

9.2 The board shall ensure that senior management implements policies that prohibit or appropriately limit activities and relationships that diminish the quality of corporate governance, such as:

9.2.1 Lending to directors and employees or officers from affiliated companies at non arms length basis;

9.2.2 Providing preferential treatment to insiders, for example, lending contrary to market terms;

9.2.3 Improper use of a bank's property and/or information;

9.2.4 Unfair dealing with customers/clients, employees, suppliers, competitors and other stake holders; or

- 9.2.5 Allowing the delinquency of loans to board members.
- 9.3 The board shall ensure that a policy is in place that encourages employees to freely communicate concerns about illegal, unethical, unprofessional or questionable practices to the board or an independent committee thereof, as well as to senior management, without fear of reprisal. This process shall include an option for employees to make their concerns known anonymously.
- 9.4 The board of every institution shall adopt a written code of ethics that sets out explicit expectations for ethical decision making and personal behaviour by all board members and employees with respect to conflicts of interest, which include circumstances such as a director participating in board discussion and voting on matters in which the director has a personal or vested interest.
- 9.5 The board shall ensure that;
- 9.5.1 Every code of ethics includes measures for dealing with breaches of the code;
- 9.5.2 It reviews the code of ethics at least annually;
- 9.5.3 Management has in place a system to implement the institution's code of ethics and to report to the board on the record of compliance at least annually;
- 9.5.4 Management communicates the institution's code of ethics to all employees and provides employee training after every review.
- 9.6 An institution shall publish its code of ethics and make them accessible to all officers/persons required to observe them in the most effective manner.
- 9.7 The annual report shall include information about the steps taken to comply with the code, including as appropriate any serious instances of unethical behaviour and any action(s) taken.
- 9.8 Every institution shall avail a copy of its code of ethics to the RBM on request.
- 9.9 Directors and officers who have an interest in a transaction to which the institution is an actual or potential party are required to disclose their interest to the board. It is the responsibility of directors to scrutinize their transactions and outside business interests and relationships and to make immediate disclosure in writing of any potential conflicts. Disclosure is to be made as soon as the director becomes aware of the conflict. This interest which encompasses circumstances such as a director participating in board

discussion and voting on matters in which the director has personal interest can include but is not limited to the following:

- 9.9.1 Being the other party to the contract;
- 9.9.2 Acting as a representative or agent of the other party;
- 9.9.3 Being a shareholder or serving as a director, trustee, partner or employee of the other party;
- 9.9.4 Being a financier of the other party;
- 9.9.5 Having a close relation such as a spouse, son or daughter who is any of the above;  
or
- 9.9.6 Having a close relation in a senior management position. In addition to any disclosures made above, each director at the beginning of each financial year, will submit a 'disclosure statement' setting forth all business relationships as of the date of the statement and a summary of transactions during the preceding financial year, which might be considered to present issues of conflict of interest.
- 9.10 For a transaction undertaken by a director to be valid, a majority of the disinterested directors shall approve the transaction.
- 9.11 An institution shall ensure that all information addressed to clients or potential clients, such as information about the nature and cost of services provided or recommendations regarding financial instruments and investment strategies are clear, fair and not intentionally misleading.

## **10.0 REPORTING AND DISCLOSURE**

### **Principle VII**

*The board shall demand integrity both in financial reporting and in timeliness, accuracy and balance of disclosures on the institution's affairs.*

### **Guidelines**

- 10.1 It shall be the board's responsibility to ensure that the institution's financial statements fairly present the state of affairs of the institution as at the end of the financial year and the

- profit or loss and cash flows for the reporting period.
- 10.2 It shall be the responsibility of the external auditor to report on whether the financial statements are truly and fairly presented in accordance with the Companies' Act.
  - 10.3 The board shall attest in a statement on the adequacy of accounting records and effectiveness of the system of internal controls and risk management, and this statement shall be included in the annual report.
  - 10.4 The annual report shall include a statement confirming that appropriate accounting policies supported by reasonable and prudent judgments and estimates have been used consistently.
  - 10.5 The annual report shall also state whether the International Financial Reporting Standards have been adhered to or if there has been any departure in the interest of fair presentation, this shall not only be disclosed and explained but quantified.
  - 10.6 The annual accounts shall give the institutions corporate social responsibility and activities both negative and positive.
  - 10.7 The annual report shall state whether these corporate governance guidelines have been adhered to or, if not, where there has not been compliance the institution shall give reasons.
  - 10.8 The board should ensure that the institution's corporate governance framework is complemented by an effective approach that addresses and promotes the provision of analysis or advice by analysts, brokers and others, that is relevant to decisions by investors, free from material conflicts of interest that might compromise the integrity of their analysis or advice.

## **11.0 TRANSPARENCY**

### **Principle VIII**

*Transparency is essential for sound and effective corporate governance. Transparency will ensure that shareholders, other stakeholders and market participants effectively monitor and properly hold the board of directors and senior management accountable.*

### **Guidelines**

- 11.1 Where banks have complex shareholding structures that may foster opacity in a manner that impedes effective market and supervisory oversight, appropriate disclosures shall be made to

facilitate market discipline as ownership transparency is central to the effectiveness of external governance.

- 11.2 Accurate disclosures in the annual report shall be made in the following areas:
  - 11.2.1 Basic organisational structure; major share ownership and voting rights, beneficial ownership, major shareholder participation on the board or in senior management positions;
  - 11.2.2 Board and senior management structure with qualifications and experience;
  - 11.2.3 Nature and extent of transactions with affiliates and related parties including any institutional matters for which members of the board or senior management have material interests either directly, indirectly or on behalf of third parties;
  - 11.2.3 Remuneration policy for members of the board and information about board members, including their qualifications, the selection process, other company directorships and whether they are regarded as independent by the board; and
  - 11.2.4 Foreseeable risk factors.
- 11.3 Banks shall establish clear policies when operating:
  - 11.3.1 through complex corporate structures such as corporate trusts or special purpose vehicles or any corporate structures that impair transparency;
  - 11.3.2 in offshore financial centres or jurisdictions that have secrecy laws or weak enforcement mechanisms or any other jurisdiction that impairs transparency; and
  - 11.3.3 A policy formulated under this section shall ensure that:
    - I. the institution's operations in the circumstances stated in 12.1 and 12.3 comply with relevant laws and regulations and facilitate effective supervision; and
    - II. the board considers the appropriateness of and sets limits for operations in such jurisdictions or the use of such structures; and senior management identifies and manages the full range of risks associated with such structures or activities.

## 12.0 **REMUNERATION**

### **Principle IX**

*The remuneration of directors and executives shall be transparent, fair, and reasonable.*

### **Guidelines**

- 12.1 The board shall have a clear policy for setting remuneration of executives and non-executive directors at levels that are fair and reasonable in a competitive market for the skills, knowledge, experience, nature and size of the institution.
- 12.2 Every institution shall provide clear disclosure of its remuneration and bonus scheme policies, level and mix of remuneration and bonus, and the procedure for setting the same in the annual report.
- 12.3 Executive directors' remuneration shall be clearly differentiated from that of non-executive directors.
- 12.4 Where executive directors' remuneration packages include an element that is dependent on individual performance as well as the institution's performance, such schemes should always strike a balance that ensures attainment of corporate objectives in the short, medium and long term.
- 12.5 Preferably, every institution should appoint a remuneration committee, consisting entirely or mainly of non-executive directors. The remuneration committee shall make recommendations to the board with agreed terms of reference on the institution's framework of executive remuneration and to determine specific remuneration packages for each of the executive directors.
- 12.6 The remuneration committee shall be chaired by a non-executive director. The chief executive officer may, at the invitation of the committee, attend meetings to provide input on the remuneration of the other executives. However, a chief executive officer shall play no part in the decisions regarding his remuneration.
- 12.7 Every institution shall provide full disclosure in the annual report of director remuneration on an individual basis, giving details of earnings, share options, restraint payments and any other benefits.

12.8 The remuneration committee shall play an integral part in succession planning for management.

## **13.0 RISK MANAGEMENT**

### **Principle X**

*Banks shall have corporate governance structures that promote effective identification, measurement, monitoring and control of all material risks. The board shall regularly verify that the institution has appropriate processes that identify, measure, monitor and control risks.*

### **Guidelines**

13.1 The board shall ensure that there are risk management policies in place.

13.2 The board shall require management to implement adequate risk management system to identify, measure, monitor, control and report all risks associated with the institution. The risk management system should be supported by a system of sound internal controls.

13.3 The board shall include in its annual report information on risk management and internal controls.

13.4 The board shall ensure management facilitates training programmes at least annually in risk management for thorough understanding of risk and the means by which it is managed.

13.5 The board shall ensure that management facilitates training programmes for directors and senior management to enable them to have a robust understanding of the nature of the business, nature of risks, consequences of risks being inadequately managed, and an appreciation of the techniques for managing risks effectively.

13.6 The board shall maintain a structure which requires regular reporting to senior management and to the board on the nature and magnitude of risks the institution is exposed to and the structures to control these risks, including a regular assurance to the board that all risk management systems and internal controls are being properly applied at all times.

13.7 The board risk management committee should maintain records of all its meetings, in particular records of discussions on key deliberations and decisions taken.

- 13.8 The board shall include a statement in the annual report that the directors are satisfied to the best of their ability, that all material risks are being managed effectively.
- 13.9 The board shall have a policy in place requiring risk management systems and internal controls to be subjected to periodic external reviews as determined by institution's risk profile and for the results of the reviews to be reported to the board.
- 13.10 The board shall ensure that management considers the compliance function as a part of the overall risk management framework and submits compliance reports to the board on a quarterly basis.
- 13.11 The board shall periodically review and approve risk exposure limits to conform to any changes in strategies, products and market conditions.
- 13.12 The board shall ensure that duties are segregated in order to avoid operational risks. The board may specify the methods of authorisation, limits and delegation as well as a dual control system and the four eyes principle to ensure accuracy of risk exposure limits.
- 13.13 The board shall ensure management uses its influence and moral suasion to promote good governance among the institution's corporate customers, thereby improving their performance and reducing their risk, which would benefit the banks themselves, and ultimately the wider economy.

## **14.0 INTERNAL AUDIT<sup>3</sup>**

### **Principle XI**

*Internal audit provides assurance that internal controls in place are adequate to mitigate risks; organizational goals and objectives are met and corporate governance processes are effective and efficient.*

### **Guidelines**

- 14.1 Internal audit shall have its purpose, authority and responsibility defined in an internal audit

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<sup>3</sup> Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve effectiveness of risk management, control and governance processes.

- charter.
- 14.2 The internal audit charter shall include among other issues, the following;
- 14.2.1 Internal audit's role and responsibility for governance, risk management, consulting services, and fraud investigations, etc.;
- 14.2.2 The right for the chief internal auditor to have unrestricted access to the audit committee chairperson, employees, facilities and records of the institution;
- 14.2.3 That the internal audit function reports directly to the board of directors or its audit committee in order to ensure independence from management;
- 14.2.4 That the chief internal auditor has a right to attend audit committee meetings;
- 14.2.5 That the chief internal auditor meets with the audit committee at least once a year.
- 14.3 Banks shall ensure that the internal audit function is properly established with adequate authority, scope and resources to enable them to operate professionally and proficiently in line with the internal audit charter standards as issued by the Institute of Internal Auditors or internationally recognized professional bodies.
- 14.4 Internal audit shall be performed by professionals with an in-depth understanding of the business, culture, systems and processes of the institution. *The internal audit function can either be in-house, outsourced to a reputable accounting/auditing firm, or performed by a major shareholder, holding company or parent company with an internal audit staff.*
- 14.5 Banks shall put in place robust internal audit procedures, with appropriate reporting lines to the board of directors, and with oversight by the audit committee of the board.
- 14.6 Internal auditors shall develop an annual work plan which must be approved by the audit committee and must include for each assignment the scope, objectives, timing and resources.
- 14.7 During the execution of internal audit, internal auditors shall identify, analyse, evaluate and record sufficient information to achieve the internal audit objectives and once the audit is completed, results shall be communicated accurately and timely. The board shall ensure that management has follow up mechanisms to ensure that recommendations made in internal audit reports are dealt with in a timely manner and that corrective actions have been taken on deficiencies noted in the audit.
- 14.8 Internal auditors shall not assume any operational responsibilities as this would impair their objectivity.
- 14.9 Non-executive directors of the board shall meet in the absence of management at least annually

with external auditors, head(s) of internal audit, compliance and legal functions.

14.10 The board audit committee should approve the appointment, resignation or dismissal of the head of internal audit.

## **15.0 INTERNAL CONTROL<sup>4</sup> COMPLIANCE**

### **Principle XII**

*Internal controls encompass policies, procedures, limits, processes, culture, tasks and other aspects of an institution that support the achievement of the entity's objectives and mission. Internal controls facilitate the efficiency of operations, contribute to effective risk management, assist compliance with applicable laws and strengthen capacity to respond appropriately to business opportunities.*

### **Guidelines**

15.1 Development and implementation of an adequate and sound system of internal controls is the responsibility of senior management. The board of directors is ultimately responsible for ensuring that such a system is established, implemented and maintained.

15.2 The board shall review at least annually the system of internal controls to determine whether it works to expectation and to ensure it remains appropriate.

15.3 The audit committee shall ensure that the institution complies with regulatory requirements, including prudential requirements, taxation rules and various reporting obligations. The corporate governance framework shall therefore include systems for ensuring that all statutory and regulatory requirements are being complied with, and to highlight potential or actual breaches as and when they occur.

## **16.0 EXTERNAL AUDITORS**

### **Principle XIII**

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<sup>4</sup> Any action taken by management, the board and other parties to manage risk and increase the likelihood that objectives and goals will be achieved.

*The board shall ensure the quality and independence of the external audit process.*

## **Guidelines**

- 16.1 The board through its audit committee shall acquaint itself fully with the responsibilities of external auditors and be rigorous in its selection of auditors on professional merit. Any auditor so appointed shall be approved by the RBM in line with provisions of the Banking Act.
- 16.2 The board shall satisfy itself that there is no relationship between the auditor and the institution or any related person that could compromise the independence of the auditor, and shall require confirmation of this from the auditor.
- 16.3 The board shall facilitate full and frank dialogue among its audit committee, the external auditors, and management.
- 16.4 The board shall include in the annual report the amount of fees paid to the auditors by the institution and its affiliates and clearly distinguish audit and non-audit fees.
- 16.5 An auditing firm that provides auditing services may be engaged to provide other non-audit work subject to prior approval by the audit committee to avoid possible conflicts of interest and to ensure independence and objectivity of audit work. However it is prohibited for the external auditor of a bank to perform executive management duties, secretarial duties and prepare its accounts.
- 16.6 The board shall explain in the annual report what non-audit work was undertaken if any, and why this did not compromise auditor independence.
- 16.7 Banks shall strive for efficient audit processes using external auditors in combination with the internal audit function.
- 16.8 Where management letters are issued, they shall be reviewed, acted on and incorporated into the internal audit work plan.
- 16.9 The institution's external audit shall not be performed by the same audit engagement partner for more than five consecutive years in order to mitigate the threat of over-familiarity. Furthermore, the individual shall not serve as engagement partner until a period of two years has elapsed.

## **17.0 STAKEHOLDER INTERESTS**

## **Principle XIV**

*The board shall respect the interests of stakeholders within the context of the institution's ownership and its fundamental purpose.*

### **Guidelines**

- 17.1 The board shall have clear written policies for the institution's relationships with significant stakeholders, bearing in mind distinctions between public, private and government ownership.
- 17.2 The board shall regularly assess compliance with these policies to ensure that the conduct towards stakeholders complies with the code of ethics and the law and that it is within broadly accepted social, environmental, and ethical norms, generally subject to the interests of shareholders.
- 17.3 Banks shall include in their annual report information of their activities, performance and how they have served the interests of their stakeholders.
- 17.4 Banks shall include in their annual report the nature and extent of their social activities, ethical, safety, health and environmental management policies and practices. The board must determine what is relevant for disclosure, having regard to the institution's particular circumstances.

## **18.0 BOARD RELATIONSHIP WITH SUPERVISORS**

### **Principle XV**

*The Board shall maintain an open relationship with the RBM which promotes mutual trust and confidence.*

### **Guidelines**

- 18.1 The board shall:
- 18.1.1 Understand the regulatory environment within which the bank operates;
  - 18.1.2 Require appropriate follow-up on recommendations and any deficiencies identified by

supervisors, including follow up with senior management to determine if weaknesses identified are indicators that similar deficiencies exist elsewhere;

18.1.3 Consider regulatory findings in its on going evaluation of senior management, recognizing that the primary responsibility for identifying weaknesses rests with the board and management; and

18.1.4 Be open to sharing with supervisors information pertaining to supervisory oversight of the institution.

## **APPENDICES**

### **APPENDIX I: Guidance on board of directors' performance evaluation**

The following are some of the questions that should be considered in a performance evaluation. They are however, by no means definitive or exhaustive, and individual banks should tailor questions to suit their own needs and circumstances.

The responses to these questions and others should enable boards to assess how they are performing and to identify how certain elements of their performance areas might be improved.

#### **Board Evaluation**

- Have any performance objectives been set for the board?
- How well has the board performed against any performance objectives that have been set?
- What has been the board's contribution to the development, determination, testing and monitoring of the bank's strategy?
- What has been the board's contribution to ensuring robust and effective risk management?
- Is the composition of the board and its committees appropriate, with the right mix of knowledge and skills to maximize performance in light of current and future strategy? Are inside and outside the board relationships working effectively?
- How has the board responded to any problems or crises that have emerged and could or should these have been foreseen?
- Are the matters specifically reserved for the board the right ones?
- How well does the board communicate with the management team, company employees and others? How effectively does it use mechanisms such as the AGM and the annual report?
- Is the board as a whole up to date with latest developments in the regulatory environment and the market?
- Has the board developed or ensured that the bank has a workable succession plan?

- How effective are the board's committees? (Specific questions on the performance of each committee should be included such as, for example, their role, composition, attendance and interaction with the board).

The processes that help underpin the board's effectiveness should also be evaluated e.g;

- Is appropriate, timely information of the right depth and quality provided to the board and is management responsive to requests for clarification or amplification? Does the board provide helpful feedback to management on its requirements?
- Are sufficient board and committee meetings of appropriate length held to enable proper consideration of issues? Is time used effectively?
- Are board procedures conducive to effective performance and flexible enough to deal with all the eventualities?
- Are new Directors properly oriented to the bank and their roles, responsibilities and expectations?

### **Chairman and Directors' Evaluation**

In addition, there are some specific issues relating to the chairman, which should be included as part of an evaluation of the board's performance e.g.:

- Is the Chairman demonstrating effective leadership of the board?
- Are relationships and communication with shareholders well managed?
- Are relationships and communication with the board constructive?
- Are the processes for setting the agenda working? Do they enable board members to raise issues and concerns?
- Is the Company Secretary being used appropriately and to maximum value?

The Chairman and other members should consider the following issues and the individual concerned should also be asked to assess themselves. For each director:

- How well prepared and informed are they for board meetings and is their attendance satisfactory?
- Do they demonstrate willingness to devote time and effort to understand the company and its business and a readiness to participate in events outside the boardroom such as site visit?

- What has been the quality and value of their contributions at board meetings?
- What has been their contribution to development of strategy and to risk management?
- How successfully have they brought their knowledge and experience to bear in the consideration of strategy?
- How effectively have they probed to test information and assumption? Where necessary, how resolute are they in maintaining their own views and resisting pressure from others?
- How effectively and proactively have they followed up their areas of concern?
- How effective and successful are their relationships with fellow board members, the Company Secretary and Senior Management? Does their performance and behaviour engender mutual trust and respect within board?
- How actively and successfully do they refresh their knowledge and skills and are they up to date with;
  - The latest developments in areas such as corporate governance framework and financial reporting?
  - The industry and market conditions?
- How well do they communicate with fellow board members, Senior Management and others, for example shareholders? Are they able to present their views convincingly yet diplomatically and do they listen and take on board the views of others.
- Do they or their affiliates have obligations to the bank that may affect their objectivity? In particular, are there any advances or loans to a director less than current?
- Do they have any litigation in or outside our jurisdictions that raise issues of fitness or propriety as director?