Corporate Governance Guidelines For Public Interest Companies

Introduction

During the past decades freedom in all aspects of business activities has increased significantly thus creating more opportunities for entrepreneurs. Increased freedom means increased responsibility. Enterprises must show respect for their shareholders as well as for other stakeholders and indeed society as a whole. The manner in which company directors promote and control their company's operations, that is, the way they exercise their stewardship, is not just a matter of interest to their shareholders, but is a matter of public interest too. Mutual trust between the public and the business community is the key to improved competitiveness.

The aim of these guidelines is to:

- advance best practice in corporate governance in Malta;
- make it easier for directors and managers to fulfill their duties and assist them in advancing the growth and development of the companies they are entrusted with directing;
- ensure public confidence in enterprises and business activities in general; and
- strengthen trust between investors, directors and managers.

These guidelines are applicable to companies having an impact on the public in general. Public interest companies are thus companies whose operations affect a substantial sector of society. These companies should not only act in the interests of their shareholders but also in the communal interest.

A 'public interest company' means any one of the following three types of companies:

(a) a regulated company; or
(b) a company that has issued debt securities to the public and whose securities are not admitted to listing on a Recognized Investment Exchange; or
(c) a government-owned entity established as a limited liability company.

A 'regulated company' means a company authorised to provide a financial or a utility service and which is either a large private company or a public company, but excluding:

- collective investment schemes;
- companies which do not hold or control clients' money;
- companies which already have an obligation to segregate clients' funds in separate accounts.

A large private company means a company which is defined under Article 209 of the Companies Act and moreover which on its balance sheet date exceeds the limits of two of the three following criteria:

- balance sheet total - one million one hundred thousand Maltese liri;
- turnover - two million two hundred thousand Maltese liri;
- average number of employees during the accounting period - fifty.

A 'public company' means a company which is not a private company in terms of the Companies Act.

These companies should aim to adopt these guidelines of corporate governance and to highlight adherence thereto in the Annual Report.

Nothing contained in these Guidelines should be deemed to override the general rules, laws and principles which regulate public interest companies but these should be considered as a general framework to support good governance within the Maltese financial sector.

In an increasingly globalized world economy where competition is intense, the adoption of good corporate governance guidelines can make a difference in the way companies are managed and perceived, both domestically and within the international scenario.

GUIDELINE 1: THE BOARD

A company should be headed by an effective board, which should lead and control the company.

1.1 The board should be composed of persons who are fit and proper to direct the business of the company. The concept of fit and proper requires directors to be honest, competent and solvent persons.

1.2 It is one of the board's main responsibilities to promote the success of the company by directing and supervising the company's affairs and management to enhance shareholders' value.

1.3 The shareholders, as the owners of the company, have the jurisdiction and discretion to appoint or remove directors on the board. The process of appointment should be transparent and conducted at properly constituted shareholder meetings where the views of the minority can be expressed.

1.4 All directors are required to provide leadership, integrity and judgment in directing the company.

1.5 All directors should:

1.5.1 exercise prudent and effective controls which enable risk to be assessed and managed in order to achieve the continued prosperity of the company;

1.5.2 be accountable for all actions or omissions attributable to them or their delegates;

1.5.3 determine the company's strategic aims and the organizational structure;

1.5.4 regularly review management performance and ensure that the company has the appropriate mix of financial and human resources to meet its objectives and to improve the economic and commercial prosperity of the company;

1.5.5 set the company's values and standards in order to enhance and safeguard the interests of shareholders;

1.5.6 act with integrity and due diligence while discharging their duties as directors and in particular in the decision and policy-making process of the company, which should be reflected in all company's dealings and at every level of the organization; and

1.5.7 exercise accountability to shareholders and be responsible to other relevant stakeholders.

1.6 Leadership can only come about if the directors, individually and collectively, are of the appropriate calibre, with the necessary skills and experience to contribute effectively to the decision-making process.

1.7 Directors therefore should:

1.7.1 acquire a broad knowledge of the business of the company;

1.7.2 be aware of and be conversant with the statutory and regulatory requirements connected to the business of the company;

1.7.3 allocate sufficient time to uphold their responsibilities; and

1.7.4 regularly attend meetings of the board.

1.8 In cases when a director is unable to acquiesce in a decision of the board because a proposed course of action is not deemed to be in accordance with his statutory or fiduciary duties and responsibilities and all reasonable steps have been taken to resolve the issue, the director may feel that resignation may be a better alternative than acquiescence. In such instances, the shareholders are entitled to an honest account of any such disagreements between directors.

GUIDELINE 2: THE CHAIRMAN OF THE BOARD

There should be a clear division of responsibilities at the head of the company between the running of the board and the executive responsibility for the running of the company's business.

2.1 The chairman has a pivotal role to play in helping the board achieve its full potential. He should encourage every director to play a full and constructive role in the affairs of the company.

2.2 The chairman is responsible to:

2.2.1 lead the board and set its agenda;

2.2.2 ensure that the directors of the board receive precise, timely and objective information so that they can take sound decisions and effectively monitor the performance of the company;

2.2.3 ensure effective communication with shareholders; and

2.2.4 encourage active engagement by all members of the board for discussion of complex or contentious issues.

GUIDELINE 3: DIRECTORS

The board should be composed of persons who as a group, have the required diversity of knowledge, judgment and experience to properly complete their tasks. This may require the inclusion of a number of non-executive directors (including independent non-executives).

3.1 The exact composition and balance on a board will depend on the circumstances and business of each enterprise. Companies should ensure a balance such that no individual or small group of individuals can dominate the board's decision-making.

3.2 A director is considered to be independent when he is free from any business, family or other relationship – with the company, its controlling shareholder or the management of either – that creates a conflict of interest such as to jeopardize exercise of his free judgment.

3.3 A 'non-executive director' is a director who is not engaged in the daily management of the company. A non-executive director has an important role in overseeing executive or managing directors and dealing with situations involving conflicts of interests.

3.4 Non-executive directors and executive directors have as board members the same duties and responsibilities in terms of law. However, as the non-executive directors are not involved in the day-to-day running of the business, they can bring fresh perspectives and contribute more objectively in supporting as well as constructively challenging and monitoring the management team.

3.5 The company should appoint non-executive directors of sufficient calibre whose independence and standing would offer a balance to the strength of character of a chairman. Where the roles of the chairman and chief executive officer are combined, it is important that the non-executive directors are able to bring an independent judgment to bear on the various issues brought before the company.

3.6 Non-executive directors should be free from any business or other relationship, which could interfere materially with the exercise of their independent and impartial judgment.

3.7 Each director should apply to his duties the necessary time and attention, and should undertake to limit the number of any directorships held in other companies to such an extent that the proper performance of his duties is assured.

3.8 Non-executive directors should:

- 3.8.1 constructively challenge and help develop proposals on strategy;
- 3.8.2 monitor the reporting of performance;
- 3.8.3 scrutinize the performance of management in meeting agreed goals and objectives; and
- 3.8.4 satisfy themselves on the integrity and financial information and that financial controls and risk management systems are well established.

GUIDELINE 4: THE RESPONSIBILITIES OF THE BOARD

The board has the first level responsibility of executing the four basic roles of corporate governance namely: accountability, monitoring, strategy formulation and policy development.

4.1 The board should regularly review and evaluate corporate strategy, major operational and financial plans, risk policy, performance objectives and monitor implementation and corporate performance within the parameters of all relevant laws, regulations and codes of best business practice.

4.2 The board should clearly define its level of power and ensure that it is known by all directors and the senior management of the company. Delegation of authority to management should also be clear and unequivocal. Independently of any powers and functions that the directors may from time to time validly delegate to management, it remains a fundamental responsibility of directors to monitor effectively the implementation of strategy and policy by management.

4.3 The board should apply high ethical standards and take into account the interests of stakeholders. Its members should act:

4.3.1 responsibly and with the highest degree of integrity when exercising independent objective judgment; and

4.3.2 on a fully informed basis, in good faith, with due diligence and in the best interests of the company and its shareholders.

4.4 The board should:

4.4.1 define in clear and concise terms the company's strategy, policies, management performance criteria and business policies which can be measured in a precise and tangible manner;

4.4.2 establish a clear internal and external reporting system so that the board has continuous access to accurate, relevant and timely information such that the board can discharge its duties, exercise objective judgment on corporate affairs and take pertinent decisions to ensure that an informed assessment can be made of all issues facing the board;

4.4.3 continuously assess and monitor the company's present and future operations, opportunities, threats and risks in the external environment and current and future strengths and weaknesses;

4.4.4 recognise and support enterprise and innovation within the management of the company. The board should examine how best to motivate company management;

4.4.5 seek to establish an effective decision-making process in order to develop the company's business efficiently;

4.4.6 evaluate the management's implementation of corporate strategy and financial objectives. The strategy, processes and policies adopted for its implementation should be regularly reviewed by the board using key performance indicators so that corrective measures can be taken to address any deficiencies and ensure the future sustainability of the enterprise;

4.4.7 ensure that the company has appropriate policies and procedures in place to assure that the company and its employees maintain the highest standards of corporate conduct, including compliance with applicable laws, regulations, business and ethical standards;

4.4.8 recognize that the company's success depends upon its relationship with all groups of its stakeholders, including employees, suppliers, customers and the wider community in which the company operates. The board should maintain an effective dialogue with such groups in the best interests of the company and monitor the application by management of its policies;

4.4.9 strike a balance between enterprise and control in the company; and

4.4.10 develop a succession policy for the future composition of the board of directors and particularly the executive component thereof, for which the chairman should hold key responsibility.

4.5 Upon being appointed to the board and throughout the term of their appointment, directors should ensure that they have sufficient and adequate information about the company, its affairs and their fiduciary duties, responsibilities and liabilities. It is desirable that periodic information sessions are organized to ensure that directors are familiar with, *inter alia*:

4.5.1 their statutory and fiduciary duties;
4.5.2 the company's operations and prospects;
4.5.3 the skills and competence of senior management;
4.5.4 the general business environment; and
4.5.5 the board's expectations.

4.6 The board must understand and fully appreciate the business risk issues and key performance indicators effecting the ability of the company to achieve its objectives.

4.7 The board should assess regularly any circumstances, whether actual or potential, that could expose the company or its directors to risk and take appropriate action.

4.8 The business risk and key performance indicators should be benchmarked against industry norms so that the company's performance can be effectively evaluated.

4.9 The board shall require management to constantly monitor performance and report, at least quarterly, fully and accurately on the key performance indicators to its satisfaction.

4.10 The board shall ensure that the financial statements of the company and the annual audit thereof have been completed within the stipulated time periods.

GUIDELINE 5: BOARD MEETINGS

The board should meet sufficiently regularly to discharge its duties effectively. Ample opportunity must be given to all board members during meetings to convey their opinions and discuss issues set on the board agenda so that they honour their responsibilities at all times.

5.1 The board should set procedures to determine the frequency, purpose, conduct and duration of meetings and meet regularly, at least once every quarter, in line with the nature and demands of the company's business.

5.2 The chairman is primarily responsible for the efficient working of the board. He must ensure that all relevant issues are on the agenda supported by all available information.

5.3 The board agenda should strike a balance between long-term strategic and shorter-term performance issues.

5.4 The attendance of board members should be reported to shareholders at annual general meetings.

5.5 Notice of the dates of the forthcoming meetings together with the supporting material should be circulated well in advance to the directors so that they have ample opportunity to appropriately consider the information prior to the next scheduled board meeting. Advance notice should be given of ad hoc meetings of the board to allow all directors sufficient time to re-arrange their commitments in order to be able to participate.

5.6 Conduct of board meetings by the chairman should facilitate and encourage the presentation of views pertinent to the subject-matter.

5.7 After each board meeting and before the next meeting, minutes that faithfully record attendance and decisions should be prepared and made available to all directors as soon as practicable after the meeting.

GUIDELINE 6: INFORMATION AND PROFESSIONAL DEVELOPMENT

The board should:

- ***actively participate in the appointment of senior management;***
- ***ensure that there is adequate training in the company for management and employees; and***
- ***establish a succession plan for senior management.***

6.1 Boards should actively consider the establishment and implementation of appropriate schemes to recruit, retain and motivate high quality executive officers and the management team.

6.2 Senior management should ensure that systems are in place:

6.2.1 to provide for the development of the management and employees generally and to provide for adequate training in the company;

6.2.2 to ensure staff receive adequate and relevant training so that the company remains competitive; and

6.2.3 to monitor management and staff morale.

GUIDELINE 7: RELATIONS WITH SHAREHOLDERS

The board shall serve the legitimate interests of the company and account to shareholders fully. Companies should use the general meeting to communicate with shareholders.

7.1 The board should endeavour to protect and enhance the interest of both the company and its shareholders, present and future. The company should therefore provide shareholders with regular, timely, accurate, comprehensive and comparable information in sufficient detail to enable investors to make informed investment decisions.

7.2 The board shall utilize the annual general meeting of the company to communicate effectively with the shareholders. It shall also ensure compliance with Company Law provisions regulating the convening of extraordinary general meetings.

7.3 The board should:

7.3.1 always ensure that all holders of each class of capital are treated fairly and equally; and

7.3.2 act in the context that its shareholders are constantly changing and consequently, decisions should take into account the interests of future shareholders as well.

7.4 Shareholders must appreciate the significance of participation in the general meetings of the company and particularly in the election or appointment of directors. They should continue to hold directors to account for their actions, their stewardship of the company's assets and the performance of the company.

7.5 The agenda for general meetings of shareholders and the conduct of such meetings must not be arranged in a manner to frustrate valid discussion and decision-taking.

7.6 A detailed explanatory memorandum should accompany all proposals put before an extraordinary general meeting or proposals considered as extraordinary business and it must be provided well in advance of the meeting with adequate time within which shareholders can evaluate it.

7.7 Provision must be made for shareholders who do not attend a general meeting to appoint a proxy of their choice to attend and vote on any matter either in favour of, or against, any proposal presented at a general meeting of shareholders, or to abstain.

7.8 The company should consider making available for inspection to its shareholders for a period of not less than 15 days particulars of service contracts and particulars of any contract in which a director of the company is materially interested and which is significant in relation to the business of the company and its subsidiaries taken as a whole.

7.9 The company should disclose the total of any outstanding loans granted by the company or any of its subsidiaries or the parent of such company to the directors of the company and of any guarantees provided for their benefit.

7.10 It is the directors' responsibility not to make improper use of information acquired by them by virtue of their position as a director.

7.11 The board should consider whether, from time to time, disclosure should be made by the company to other stakeholders other than its shareholders, but in other respects treating them equally as regards content and timeliness.

GUIDELINE 8: CONFLICTS OF INTEREST

Directors' primary responsibility is always to act in the interest of the company and its shareholders as a whole irrespective of who appointed them to the board.

8.1 A director should avoid conflicts of interest at all times and shall make a declaration at the first board meeting if he is aware that he has an actual conflict of interest.

8.2 Should an actual or potential conflict arise during the tenure of a directorship, a director must disclose the conflict in full and in time to the board and the board shall determine whether or not that director should participate in the discussion. In any event, the director shall refrain from voting on the matter.

8.3 The personal interest of a director must not take precedence over those of the company and its shareholders.

8.4 A director having a continuing material interest that conflicts with the interests of the company should, following consultation with the chairman, take effective steps to eliminate the grounds for conflict. In the event that such steps do not eliminate the grounds for conflict then the director should consider resigning.

8.5 Each director should declare to the company his or her interest in the share capital of the company distinguishing between beneficial and non-beneficial interest.

GUIDELINE 9: CORPORATE SOCIAL RESPONSIBILITY

Directors should seek to adhere to accepted principles of corporate social responsibility in their day-to-day management practices of the company.

9.1 Corporate Social Responsibility is the continuing commitment by business entities to behave ethically and contribute to economic development while improving the quality of life of the work force and their families as well as of the local community and society at large. Being socially responsible means not only fulfilling legal expectations, but also going beyond compliance and investing 'more' into human capital, the environment and the relations with stakeholders.

9.2 Companies are encouraged to take up initiatives aimed at augmenting investment in human capital, health and safety issues, and managing change, while adopting environmentally responsible practices related mainly to the management of natural resources used in the production process.

9.3 Companies are expected to act as corporate citizens in the local community, work closely with suppliers, customers, employees and public authorities.

9.4 Companies are encouraged to go through material relating to the theme of corporate social responsibility and keep abreast with initiatives being taken in the local and international scenario.