

Stakeholder Consultation on Revisiting the Corporate Governance Framework for Entities Authorised by the MFSA

Ref: 01-2020

Date: 18 May 2021

Table of Contents

Table of Abbreviations.....	3
1 Introduction.....	4
2 Feedback Statement	5
2.1 General.....	5
2.2 Scope and Application.....	5
2.3 Type of Code.....	7
2.4 Explanation Required.....	9
2.5 The Board of Directors.....	10
2.5.1 The Board of Directors.....	10
2.5.2 Structure and Composition of the Board.....	11
2.5.3 Diversity.....	13
2.5.4 Appointment, Resignation, Dismissal and Removal of Directors.....	13
2.5.5 Directors’ Responsibilities.....	15
2.5.6 Board Members’ Remuneration.....	15
2.5.7 Evaluation of Board Performance.....	17
2.5.8 Board Meetings.....	17
2.5.9 Conflicts of Interest and Related Party Transactions.....	18
2.5.10 Advisors of the Board.....	20
2.5.11 Responsibilities of Functionaries and Officials.....	21
2.6 Engagement with Stakeholders.....	23
2.7 Engagement with Shareholders.....	24
2.8 Engagement with Institutional Investors.....	24
2.9 Engagement with Employees.....	25
2.10 Committees.....	26
2.11 Corporate Culture.....	27
2.12 Ethics Framework.....	28
2.13 Risk Management.....	29
2.14 Anti-Money Laundering and Combatting the Funding of Terrorism.....	30
2.15 Continuous Professional Development.....	30
2.16 Professional Indemnity Insurance.....	31
2.17 Business Continuity and Disaster Recovery.....	32
2.18 Disclosure.....	33
2.19 Compliance Statement.....	33
2.20 Corporate Social Responsibility.....	34
3 Way Forward: MFSA Code on Corporate Governance.....	36

Table of Abbreviations

AML	Anti-Money Laundering
CEO	Chief Executive Officer
CFT	Combating the Financing of Terrorism
CPD	Continuous Professional Development
CRD	Capital Requirements Directive
EU	European Union
IoD	Institute of Directors
MFSA	Malta Financial Services Authority
MiFID	Markets in Financial Instruments Directive
ML	Money Laundering
MLRO	Money Laundering Reporting Officer
MoU	Memorandum of Understanding
SME	Small and Medium-Sized Enterprises
OECD	Organisation for Economic Cooperation and Development
FT	Funding of Terrorism

1 Introduction

On the 5 February 2020, the Malta Financial Services Authority ('MFSA' or 'the Authority') issued a [Consultation Document](#) proposing a comprehensive and enforceable cross-sectoral Corporate Governance framework for all persons authorised by the MFSA, as well as listed companies.

The Authority proposed a review of the existing framework, with the intention of raising the standards, practices, and processes of Governance by the authorised/listed persons and ensuring that good Governance is considered as a top priority and embedded in firms' culture by the Board of Directors and senior management.

The main proposals concerned:

- i. Scope and application of the Code
- ii. Type of Code and its enforceability
- iii. Enhancing the effectiveness of the Board of Directors
- iv. The introduction of provisions to better engage with stakeholders, shareholders, institutional investors, and employees
- v. Revisiting the responsibilities of Functionaries and Officials
- vi. A number of provisions on different aspects of Corporate Governance, including amongst others, Committees, Corporate Culture, Ethics Framework, AML and CFT, Risk Management, etc.

Feedback was received from a wide range of industry participants, with the Authority receiving over 30 responses. Respondents included authorised entities, listed entities, associations and groups, law firms and consultancy firms.

This Feedback Statement highlights the key points of contributions received and sets out the MFSA's response and position thereto. The last section outlines the next steps that will be taken by the Authority pursuant to this project.

The contents of this document should be read in conjunction with the Consultation Document of the 5 February 2020.

2 Feedback Statement

2.1 General

The MFSA would like to thank stakeholders for the valid and detailed responses received – these were all carefully noted and taken into consideration when establishing the way forward. Whilst a number of views were expressed, it can generally be stated that the MFSA's initiative was positively received and that there was a broad agreement amongst respondents that the Corporate Governance framework in Malta should be strengthened.

The majority of stakeholders appreciated that good Corporate Governance is crucial and that the review will benefit the financial services industry and the jurisdiction in general. This notwithstanding, respondents raised a number of concerns and put forward several views and recommendations in relation to the proposed framework. These will be explained in further detail in this document.

Furthermore, the MFSA's position seeks to ensure that the highest standards of Corporate Governance are adopted within all sectors, including, but not limited to, the financial services market.

In its [Strategic Plan 2019-2021](#), the Authority committed "to enhance Governance, Culture and Conduct across all different sectors, contributing towards strengthened accountability, market trust and transparency." The Authority also intends to enhance awareness of best Corporate Governance practices in several ways, including but not limited to, communications, information sessions and effective engagement with market participants.

2.2 Scope and Application

The Authority proposed the introduction of a principles-based Corporate Governance Code applicable to all entities authorised by the MFSA and Listed Companies, whilst retaining the possibility of having sector-specific guidance notes and/or MFSA Rules, supporting the Corporate Governance Code. The application of the proportionality principle, ensuring that a 'one size fits all' approach is not adopted, was considered to be central to the Authority's proposal.

The Authority intends to establish the proposed Code to complement the existent national and European frameworks, and should any conflict arise between existent legislation (and any Regulations or Rules issued thereunder) and the Code, the former will take precedence over the latter.

2.2.1 Feedback Received

The majority of respondents welcomed the Authority's commitment to revisit the existent framework and the proposal to issue a comprehensive principles-based Corporate Governance Code, highlighting that embracement of these principles would enhance the Governance culture and Malta's standing as a financial services jurisdiction. It was also outlined that by having one Code based on a set of common principles, cross-sectoral standards of good Corporate Governance would be easier to adopt.

This notwithstanding, retaining sector-specific guidance and rules was deemed crucial by the majority of respondents, stating that persons falling within scope of the proposed new Code are extremely diverse in nature, size, business models, also including the risks that they may be exposed to. In this respect, a “one size fits all approach” was clearly identified by the majority of respondents as not being deemed suitable.

The majority of respondents also recommended that the MFSA should establish clear criteria for determining the applicability of the proportionality principle to rules and guidelines, stating that the Authority should be pragmatic and proportionate in its approach, taking into account entities’ size, internal organisation, as well as the nature, scale and complexity of its activities.

Further clarity was also sought with respect to how the proportionality principle would be applied in practice, with some respondents pointing out that authorised entities should be allowed some flexibility, given that they are already heavily regulated by various local and European frameworks.

Citing proportionality, many respondents suggested that the Authority should exclude certain types of entities from the scope of the Code, particularly where the proposals appear not to be proportionate. These include (i) Captive Insurance Companies; (ii) Tied Insurance Intermediaries; (iii) Ancillary Insurance Intermediaries; (iv) Family Trusts; (v) Entities listed on Prospects market¹; (vi) Regulated Authorised small private companies; (vii) Non-listed entities reporting into listed entities; (viii) Entities authorised by the MFSA that do not have physical operations such as collective investment schemes and securitization vehicles; (ix) Companies that do not hold or control clients’ money; (x) Companies which already have an obligation to segregate clients’ funds in separate accounts.

Whilst a number of respondents questioned whether the benefits of introducing some of the proposed changes would be outweighed by the consequential increase in costs, other respondents welcomed the Authority’s proposal stating that the proposal would clearly set out the Regulator’s minimum requirements and expectations. In this regard, a respondent suggested that the language to be used in the Code should be clear and unambiguous.

Other respondents stated that the new Code could conflict with the existent local and EU regulatory framework. It was therefore recommended that prior to drafting the new Code, adequate consideration ought to be given to existent obligations in order to avoid duplication of requirements and conflicts that may have an impact on the actual implementation of the proposal at hand.

Further to the above, a key concern raised by respondents was in relation to the proposal of having a single Code to address Corporate Governance for both listed entities and entities. The arguments presented in this respect were that the listed and regulated entities are in many ways very different, despite overlaps in some cases. In addition, it was argued that listed entities, traded on a public market, have a responsibility towards the investing community and towards the public in general, which is different in nature to the responsibilities of regulated firms which are responsible to the public, via the Regulator. Furthermore, the sort of Corporate Governance required of a regulated entity, can, in some areas, differ significantly from that required of a listed entity.

¹ The Prospects MTF is a multilateral trading facility targeting small and medium enterprises operated by the Malta Stock Exchange. The Prospects market already places a duty and responsibility on the corporate advisor to ensure that the listed entity has a proportionate Corporate Governance structure in line with the expectations of the Listing Authority and the market. Therefore, some respondents feel that entities listed on the Prospects market should be excluded from such a Framework.

2.2.2 MFSA Position

The responses received demonstrate that stakeholders were largely in favour of the Corporate Governance framework in Malta being revisited. The Authority welcomes the support received in relation to its proposal for a principles-based framework, the application of which will be based on proportionality.

Further to the feedback received, the Authority will adopt a principles-based framework, setting out a list of core principles. In this manner, the risk of introducing provisions that are inconsistent with other regulatory instruments is expected to be mitigated.

The Authority has given due consideration to the concerns presented in relation to the proposal of having a consolidated Code covering both listed and regulated entities. In this regard, given the valid arguments presented regarding the issues that may arise in having a consolidated Code applicable to both type of entities, the Authority resolved to retain the current Codes of Governance for Listed Entities and Prospects (which may nonetheless be updated as needed by the MFSA) and issue this framework for authorised entities embedding general principles.

As specified above, the framework itself shall provide that should a conflict arise between this framework and the provisions prescribed in the applicable laws, regulations, rules or guidance notes issued by the Authority or European Supervisory Authorities, the provisions of such laws, regulations, rules or guidance notes shall prevail. This shall also cover instances where more onerous/ mandatory provisions are prescribed in the applicable regulatory framework.

Due to the varied nature of the entities, which would fall within the scope of the proposed framework and in order to ensure that the proportionality principle is applied, the principles are expected to be general, which will also include supporting provisions, explaining how the principles may be achieved. Furthermore, the principles (and supporting provisions) shall then be complemented by sector-specific rules and/or guidance notes.

The principles will be drafted in a manner that ensures that the needs of entities that differ in nature, size, complexity, operating environment, and risks posed to consumers and the overall stability and integrity of financial markets are met.

In addition, in the drafting of any principles, the Authority will also have regard to the various requirements applicable to certain authorised persons emanating from local and European frameworks in order to ensure that such provisions complement the existing regulatory frameworks.

The Authority believes that the implementation of such standards should effectively drive substantial changes in the overall Governance standards of entities.

2.3 Type of Code

The Authority proposed adopting a hybrid approach including a principles-based Corporate Governance Code, laying down core principles for good Corporate Governance standards, which would then be complemented by sector-specific rules and/or guidance notes.

It was proposed that entities would be expected to ‘apply and explain’ the core principles-based Code through a reporting framework. Furthermore, it was proposed that this would be supplemented by sector-specific rules and/or complementing guidance notes on how entities are to adhere and explain their adherence to the Code.

2.3.1 Feedback Received

Respondents’ views on the adoption of a hybrid approach, including both principles and rules and guidance notes, was generally well-received.

Respondents welcomed the flexibility which can be provided by a hybrid approach, stating that this would ensure that the most important requirements are adhered to as a common and consistent minimum cross-sectoral standard would be established, with sectoral rules and guidance which would then focus on the distinctive features of each sector and type of authorised and/or listed person.

Nevertheless, a number of respondents expressed concerns and suggested amendments. Certain respondents stated that the “apply and explain” approach, which is being proposed for the principles-based Corporate Governance Code, would cause an excessive burden in terms of costs, highlighting that certain entities may not possess the necessary resources to comply with the new requirements. These respondents identified the “comply or explain” approach as being more favourable as, in their view, the “apply and explain” approach was more rigid.

It was also recommended that the Authority should provide a clear indication of the overarching principles and what entities would be required to “apply and explain” and “comply or explain”. A respondent also suggested that the Authority may also consider a model where the focus is on core principles complemented by non-prescriptive guidelines.

2.3.2 MFSA Position

The MFSA has considered the responses put forward and will be retaining the proposed hybrid approach. Such a hybrid approach will consist of a combination of a principles-based approach, supported by a rules and guidance notes-based approach.

The Authority has also considered in detail the feedback received, highlighting that a mandatory application of the principles (that is, on an ‘apply and explain’ basis) may have a heavy impact and increase the overall costs for certain entities. However, on the other hand, the MFSA’s supervisory experience of the application of current applicable MFSA Governance Codes has shown that a “comply or explain” approach on its own does not drive significant behavioural changes.

In this respect, the MFSA is revising its position, and the list of principles will be applied on a “best effort basis”. That said, as specified above, the list of principles is expected to be complemented by either binding Rules and/or guidance notes (or sectoral specific Codes if deemed necessary) that would apply to different typesets. The List of Principles is expected to contain ‘main principles’ which will form the basic framework, setting out the material requirements for good Corporate Governance, together with supporting provisions (in the Code itself) acting as guidance of how the relevant principles could be implemented.

It is expected that whilst any provisions reflected in the MFSA Rulebooks will be binding, guidance notes will have a more discretionary application. The applicability of any sectoral Codes (i.e., apply and explain/ apply or explain/ best effort basis) that may be developed in due course will depend on the sector and type of authorisation held by the regulated entity.

The adoption of either Rules and/or guidance notes will be subject to further policy work analysis to be conducted by the MFSA in due course. Whilst certain Governance related requirements are already embedded in the MFSA Rules, the determination between i) the use of guidance notes, sectoral Codes, or else ii) whether updates would need to be effected to the Governance section of the various Rules will be dependent on the respective sector and the type of authorisation held by the entity.

The Authority believes that this approach ensures an effective, proportionate approach in the application of the list of principles, whilst also ensuring, however, that requirements that are deemed of critical importance for a certain type of entities are enforced in the Rules, or else supplemented by guidance notes and/or sectoral Codes.

2.4 Explanation Required

In the Consultation Document, the Authority stated that any explanations and disclosures which would need to be provided with respect to the application of the principles contained within the Corporate Governance Code should be concise yet sufficiently detailed to provide a clear picture of the person in question's state of affairs. It was also stated that rules to eliminate the tendency of re-using explanations already provided in previous years ('boiler plating') would be introduced.

2.4.1 Feedback Received

This proposal was positively received by the large majority of respondents as it was felt that explanations should be adequate, concise and relevant to the reporting year in question.

Certain respondents suggested that the rules regarding explanations should not be a "one-size-fits-all" and that the principle of proportionality is applied.

Other respondents stated that requiring adequate explanations would also discourage the application of a tick-box approach. Respondents highlighted that the effectiveness of the Authority's initiative would be largely impacted by the adequacy and completeness of the explanations provided.

With respect to "boiler plating", it was highlighted that an entity might be exposed to risks that do not change significantly from year to year and hence, explanations provided in previous years could be relevant for subsequent reports. A respondent also highlighted that "boiler plating" can be eliminated through proper scrutiny of Corporate Governance statements.

Some respondents suggested that the Authority should consider providing a transitory period where entities should be required to submit Governance explanations solely to the MFSA and that public disclosures should be introduced after issuing the sectoral rules. It was also proposed that the Authority should require

explanations only for those issues which are deemed sensitive, carrying out an assessment on a case-by-case basis.

2.4.2 MFSA Position

In view of the proposed change being adopted in terms of the approach in the applicability of the Code (i.e., to a 'best effort basis'), the disclosure related requirement (which would have been applicable if the Code had to be implemented on an 'apply and explain' or 'apply or explain' approach), is no longer applicable.

2.5 The Board of Directors

2.5.1 The Board of Directors

In order to enhance the role of the Board of Directors and its efficacy, the MFSA proposed requirements in relation to [i] structure and composition of the board; [ii] diversity; [iii] appointment, resignation, dismissal and removal of directors; [iv] directors' responsibilities; [v] remuneration; [vi] evaluation of board performance; [vii] board meetings; [viii] conflicts of interest and confidentiality; and [ix] advisors to the board.

The Authority also proposed a new obligation for the board to draw up a board charter that sets out its policies and procedures.

2.5.1.1 *Feedback Received*

The majority of respondents agreed that the role of the Board of Directors should be enhanced and considered the Authority's proposal to be comprehensive, while others expressed concern.

A significant group of respondents stated that principles regarding structure, composition, diversity, appointment, resignation, responsibilities, remuneration and board performance should be set out in guidelines and not rules, in order to provide entities with the opportunity to decide whether comply or otherwise, depending on their business model, size and corporate structure.

Some respondents also pointed out that certain matters - such as appointment and dismissal, directors' responsibilities and conflicts of interest - fall within the scope of the Company's Act or are included in the articles of association, and it was, therefore, suggested that in order to avoid duplication or overlap of requirements, the Company's Act should continue regulating such matters, whilst the new provisions in the Corporate Governance framework should solely complement or clarify current requirements.

Specifically, with respect to the board charter, whilst some respondents agreed with the proposal stating that this would address matters which are not functioning properly in practice, some respondents requested further clarifications, particularly on the difference between a "board charter" and "board terms of reference". Amongst such respondents, some recommended that rather than adding a new obligation requiring an additional document, guidelines on the content of Term of Reference should be issued by the Authority.

2.5.1.2 MFSA Position

The Authority acknowledges the responses received in relation to its proposal to introduce provisions aiming at enhancing the effectiveness of the Board of Directors.

With respect to the concerns raised vis-à-vis potential overlaps with the existing legal and regulatory framework and to provide further clarity, the Authority is expecting such matter to be addressed by having a framework based on core principles and supported by sector-specific complementing guidance notes and/or rules. The new framework will refer to the Companies Act and complement the obligations set out therein, limiting the duplication of current requirements.

With regard to the Board Charter, the Authority took on board the feedback received and intended to cover this aspect, in the supplementing guidance notes and / or Rules.

The Authority is cognisant that the applicability of principles regarding the Board of Directors depends on the legal structure of the various entities falling within the remit of the framework.

In the case of entities established as a Unit Trust, Limited Partnership, or any other legal form permissible to be established in terms of the regulatory frameworks, the principles will apply (to the extent possible and as applicable) to whatever body is charged with the functions of governing the entity and monitoring management.

The term “Board of Directors” as used in this section and throughout the document is meant to embrace the different models of board structures and management bodies.

2.5.2 Structure and Composition of the Board

The Authority proposed the inclusion of several requirements regarding the composition and structure of the Board of Directors within the new Corporate Governance framework.

2.5.2.1 Feedback Received

Feedback received in this respect was mixed.

The majority of respondents agreed with the proposal to require that *“the structure and composition of the board should ensure that no person or group of persons can dominate decision making”*, stating that this would enhance the proper functioning of the board. This notwithstanding, respondents noted that imposing the exact board composition may not serve the purpose, particularly if entities had to appoint extra board members to comply with the new requirements and these additional members do not provide added value to the overall composition and structure.

Furthermore, whilst some respondents agreed with the proposal of having a mix of executive and non-executive directors sitting on the board, subject to the application of the proportionality principle, others sought clarity from the Authority vis-à-vis the distinction between the roles of the executive, non-executive and independent directors. It was also submitted that the Authority should issue guidelines with respect to the

required/suggested composition of an entity's board. Some respondents also proposed that the importance of the role of independent directors should be emphasised in the new framework.

The majority of respondents did not agree with the Authority's proposal to require the appointment of a Lead Independent Director, arguing that such directors should work collectively without the need for a lead director as all directors have the same duties and liabilities, and the role of Lead Independent Director may lead to a concentration of power in the hands of one person. The few respondents who agreed with the proposal highlighted that such a person would be able to assist in sensitive board issues, increasing engagement with shareholders and other stakeholders.

A respondent pointed out that the concept of Lead Independent Director deserves to be further explored and developed since it could result in promoting transparency and neutralizing any dominance that might arise on a Board of Directors. In this respect, the importance of proportionality was also stressed.

The proposal to require the publication of an up-to-date organisational structure on entities' websites also brought mixed views from respondents. Whilst some agreed with the Authority's proposal, others thought that this would not add value.

It was also argued that this requirement already exists in many sectoral frameworks, and the introduction of the revised Corporate Governance Code would lead to duplication of disclosures. One respondent also pointed out that where an entity does not have a website, the publication of an up-to-date organisational structure highlighting all Governance roles, responsibilities or accountabilities, would not be achievable in practice.

2.5.2.2 MFSA Position

The Authority firmly believes that an effective system of checks and balances is needed in order to strengthen the effectiveness of the Board of Directors. The composition of the board should be such as to ensure that no person or group of persons can dominate decision making. In this respect, the Authority is therefore of the view that no change to its position is necessitated.

Given the overall support of respondents, the Authority will retain the principle that the composition, size, and expertise of the board should ensure adequate oversight of the operations of the entity, taking into account the nature, size and complexity of such entity. The exact composition will not be stipulated as a principle, but such requirement would be reflected either as part of the rules, guidance notes (or sectoral Codes) applicable for the various sectors, depending on the type of entity/authorisation held (as applicable).

The Authority has also considered carefully the feedback received with respect to the proposal for the appointment of a Lead Independent Director and has decided not to introduce this measure in the core principles.

Furthermore, the Authority has also reconsidered the proposal for the need to publish an up-to-date organisational structure on the entity's website, and it shall rather be including such requirement in the rules/guidance notes rather than in the list of Principles.

2.5.3 Diversity

The Authority proposed the introduction of provisions to ensure diversity on Boards of Directors *inter alia* in terms of knowledge, experience, and gender. Entities would also be required to explain their initiatives geared to enhancing diversity on their board.

2.5.3.1 Feedback Received

The majority of respondents agreed in principle with the need to ensure diversity of knowledge, experience, and gender on the Board Directors in order to ensure a more balanced composition of management bodies; however, they also emphasised that locally, the pool of persons who have the knowledge and experience to perform the role of director, is limited. Respondents highlighted that provisions which will oblige entities to achieve diversity on boards, particularly with respect to gender, would be difficult to implement.

Certain respondents expressed a preference for the publication of recommendations and guidelines, emphasizing the benefits of a diverse board structure rather than prescriptive rules. Other respondents suggested that diversity should be considered as a goal that entities must achieve and that it should be left up to each entity to establish how to reach this goal. In this regard, it was suggested that entities would be required to state, in their annual report, how diversity objectives are being met.

2.5.3.2 MFSA Position

The MFSA noted the industry's feedback that the proposal put forward in the Consultation Document may be difficult to implement by certain entities. In line with feedback received, the Authority does not intend to introduce prescriptive blanket requirements, especially in view of the varying type of entities that will fall within the scope of the framework.

In this respect, given that board diversity is increasingly being considered as an important tool for enhancing firm performance, the Authority will be including the diversity element as a provision supplementing the board composition main principle - promoting both social diversity (such as gender, race/ ethnicity and age) and professional diversity.

2.5.4 Appointment, Resignation, Dismissal and Removal of Directors

In order to enhance the transparency of the appointment process of Directors, the MFSA had proposed requiring entities to clearly set out the respective appointment and the resignation processes. It was also proposed that the Code includes a provision which would require companies to explain such appointment process and the selection criteria availed of. Reference was also made that, in this respect, companies should, *inter alia*, consider the individual's fitness and properness assessments for the role.

The Authority also proposed: [i] raising the requirements vis-à-vis competence by requiring directors to have adequate qualification/certification; [ii] requiring companies to provide an induction programme to any newly appointed director; and [iii] the issuance of a policy on multiple involvements.

Furthermore, specifically with respect to resignations, the Authority proposed the inclusion of a provision within the Code, requiring companies to explain the resignation process for directors and the succession plan as well

as the measures to mitigate key-man risk. Moreover, it was proposed that provisions on the procedure to remove/dismiss a director are included.

2.5.4.1 *Feedback Received*

The majority of respondents were supportive of the proposal put forward by the Authority to raise requirements vis-à-vis knowledge, with many sharing the MFSA's views that all directors should be adequately qualified and certified. However, some respondents argued that the introduction of a certification requirement may discourage individuals from taking on the role of a director, who, although not having academic qualifications, are fit and proper for the role.

A number of respondents requested further clarity on the Authority's interpretation of "adequate qualification/certification". Another recommended that the competence of a board should be assessed on a collective rather than an individual basis.

With respect to the Authority's proposal to issue a specific policy on multiple involvements, the majority of respondents were keen to get further clarity thereon. The limited pool of resources available on the local market was once again highlighted as a matter of concern.

Respondents provided mixed opinions on the MFSA's proposal vis-à-vis the resignation process. Whilst some respondents were of the view that having a resignation and succession policy in place should indeed be encouraged as part of entities' risk management strategy, and others considered the proposal of establishing a formal process for resignation/dismissal to be disproportionate.

2.5.4.2 *MFSA Position*

The Authority has noted the response received in relation to the appointment of directors, including raising of the requirements vis-à-vis competence by requiring directors to have adequate qualification/certification.

In this respect, the Authority will be including a principle making reference to a formal and transparent procedure regarding the appointment of new directors, which should also ensure that they possess the relevant skills, experience, and knowledge required to fulfil their responsibilities effectively. Entities will be required to, *inter alia*, consider the proposed board member's fitness and properness assessments for the role.

The Authority is maintaining its views that reference to the need to provide an induction programme to any newly appointed director is to be included in the list of Principles.

With respect to the proposals in relation to the resignation and dismissal of directors, the Authority intends to amend the principle to refer to the need for entities to have in place an effective succession plan. Managing such risks is considered to be essential towards enhancing entities' resilience and business continuity, particularly in the event of unforeseen crises or disruptions.

The Authority also remains of the view that an MFSA Multiple Involvements Policy should be issued. However, this is expected to be part of future dedicated policy work (including an industry Consultation exercise) by the Authority. The determination of the type of roles, type of entity and sectors that would fall within the scope of such policy will be part of such assessment and policy work.

2.5.5 Directors' Responsibilities

With the aim of clarifying the expectations placed on board members, the Authority is proposing that the Code contains a principle on directors' responsibilities, including [i] their joint and several liabilities; [ii] the duty to act honestly, fairly and professionally in the best interest of the company and stakeholders; as well as [iii] the consequences of breaches of their duties as directors or breaches being committed by the company of which they are director/s.

The Authority is proposing replicating Article 136A of the Companies Act within the new framework, and providing that as part of their oversight role, directors should also monitor the financial health - including capital, solvency and liquidity levels, and its status as a going concern – of the companies of which they are directors.

2.5.5.1 Feedback Received

This proposal was well-received by the majority of respondents; however, it was pointed out that, since the provisions are already encompassed in the existent regulatory framework, the proposal does not add any new safeguard/s. Respondents argued that the Code should not replicate provisions already in force, especially in areas that fall outside the MFSA's remit. It was highlighted that the liabilities and duties of directors should be regulated by corporate law, civil law, and criminal law and not by a principles-based Corporate Governance Code.

In this respect, respondents also stated that in order to avoid issues of interpretation, the provisions on directors' responsibilities within the Companies Act and those within the Code should be aligned, and in case of conflict, the Companies Act should always prevail.

In this light, some respondents suggested cross-references to laws and guidelines in order to promote awareness.

2.5.5.2 MFSA Position

The Authority has considered the feedback received. The aim of this principle is to increase awareness of directors' duties and obligations whilst establishing a common standard of conduct for all directors. In this respect, it will be including a core principle on the responsibilities of the board in executing the roles of Corporate Governance (which will also include monitoring of financial health of the company). This will be supported by provisions of how such responsibilities can be ensured.

2.5.6 Board Members' Remuneration

With the objective of enhancing transparency on the remuneration of board members, the Authority had proposed introducing provisions requiring: [i] a formal and transparent procedure for the determination of directors' pay; [ii] adequate disclosures with respect to both the procedure for the determination of directors' remuneration and the remuneration being afforded to directors; and [iii] granting shareholders the right to influence how much directors are paid, including a right to vote *ex-ante* on the remuneration policy and *ex-post* on the amount of remuneration granted to Directors in the past financial year.

2.5.6.1 Feedback Received

Respondents provided mixed views on the proposed requirements.

Some respondents agreed with the proposed introduction of a requirement for adequate disclosure of the methods adopted to determine director remuneration. Moreover, a particular respondent stated that this would ensure that inappropriate risks are not taken, furthermore stating that this would be indicative that a clear and logical process, which is supported by adequate documentation, is in place. Other respondents suggested that entities should disclose their remuneration policies on their website, suggesting that this would be beneficial to the interests of several stakeholders.

On the other hand, other respondents expressed concern that this requirement would be an extra layer of prescriptive provisions for authorised businesses which are already subject to rules on board remuneration as well as being too onerous for other types of companies, such as privately-owned small and medium firms.

A respondent suggested that the Authority should clarify the extent of the disclosure that would be required. It was also recommended that this should only apply to remuneration packages which are over certain set material thresholds. It was also suggested that different principles should be applied in relation to executive and non-executive directors.

Another respondent suggested that remuneration policies should cover remuneration to key roles within the firm and not solely directors.

Respondents also made reference to the proportionality principle, highlighting that small and medium sized enterprises should not be subject to the same level of requirements as larger firms.

A number of respondents agreed with the proposal to grant voting rights *ex-ante* on the remuneration policy; however, the majority of respondents disagreed with the proposal of providing shareholders with the right to vote *ex-post* on remuneration packages, arguing that this would encourage a short-term approach which may not be in the long-term interests of a company. One respondent also outlined that this requirement would have an impact on the availability of suitable candidates for the role of Director. It was also noted that shareholders' powers regarding remuneration are already established in the Companies Act, and that repetition in the Corporate Governance Code would be unnecessary.

2.5.6.2 MFSA Position

The Authority welcomes the feedback received and has taken note of the respondents' concerns.

Further to additional analysis together with consideration of the feedback received in this respect, this principle shall be amended to refer to 'Remuneration' in order to cover executive remuneration, besides that of board members.

Given the importance of having remuneration policies and practices that are structured in a way that supports both the entity's strategy and long-term sustainable success, the relevant principle covering the need to have in place formal and transparent procedures in relation to the determination of remuneration is considered crucial by the Authority. Accordingly, this position is being retained. With regard to the disclosure aspect of the remuneration, it has resolved that it shall be covered in the complementing rules/guidance notes rather than in the principles.

With regard to the proposal of granting shareholders the right to influence how much directors are paid, the Authority took note of the feedback received about this requirement and shall not be introducing such a requirement.

2.5.7 Evaluation of Board Performance

Similar to existing provisions in the Code of Principles of Good Corporate Governance for Listed Entities, the Authority proposed introducing a provision requiring the board to make an evaluation of its own performance and that of its committees. It was also proposed that an assessment of the individual performance of every board member should be carried out.

2.5.7.1 *Feedback Received*

Overall, the majority of respondents agreed with the proposals put forward by the Authority; however, some disagreed with the requirement of publishing board performance outcomes, stating that this information ought to be retained confidential and provided solely to the Authority, given its commercial sensitivity.

Other respondents requested clarifications on the proposal, specifically on (i) the meaning of board performance; (ii) the frequency of evaluations; and (iii) who will carry out such assessments.

One particular respondent also suggested that the assessment should be performed every three years by a qualified individual; other respondents recommended that, in order to avoid subjectivity, the evaluation of board performance should be part of an assessment undertaken by the entity's internal audit function and based on the proportionality principle.

With respect to the proposal regarding the evaluation of individual directors' performance, it was suggested to leave the decision as to whether to evaluate directors individually to the company's discretion.

2.5.7.2 *MFSA Position*

The Authority recognises the importance of regular assessment and evaluation of the performance of the board and its committees as this enhances effectiveness and engagement. Furthermore, board evaluations may represent an important tool for assessing and improving board performance.

The new framework will accordingly include a principle regarding the evaluation of the board and its committees. The provisions supporting this principle will include guidance on how this evaluation should be carried out, by who and where it may be disclosed. This should allow flexibility to the different entities on how to perform such an assessment.

With respect to the related evaluation of individual board members' performance, the Authority has carefully considered feedback received and has agreed not to introduce such measure in the list of principles.

2.5.8 Board Meetings

The Authority had proposed a number of requirements in this respect as follows: [i] that board meetings should be held, at least, quarterly; [ii] that the procedure for board meetings is included in companies' Memorandum and Articles; [iii] that board packs should be circulated prior to the meeting and within adequate timeframes and [iv] that board meetings minutes should be drafted in a manner which allows the user to understand (a) the rationale underlying any decision that was taken and any underlying discussions, including any specific

concerns raised by individual directors; and (b) that the board has considered the impact of their decisions on the company's various stakeholders.

2.5.8.1 Feedback Received

The majority of respondents agreed with the proposal put forward by the Authority to require a minimum number of board meetings per year. They also considered that these provisions would clarify the Authority's expectations thereon.

Respondents also put forward a number of suggestions as follows: [i] board meetings, calendar and agenda should be circulated well in advance, with board packs distributed at least one week prior to the meeting; [ii] board papers should be circulated to directors in a timely manner so as to ensure an adequate review ahead of the meeting; [iii] a board minutes template to be published by the Authority so that guidance is provided on the expected standard; [iv] board meetings are not to be scheduled too late from the relevant reporting period, for example, within 15 to 30 days from the end of the reporting period; [v] there should be a requirement to disclose statistics of attendance to board meetings.

Some respondents also suggested that in line with the principle of proportionality, entities should be allowed to set the number of their meetings according to their needs, bearing in mind that the selection of the frequency will be subject to scrutiny by the Regulator. Some respondents felt that certain requirements, such as the timeframes around the distribution of board packs, should feature as best practice principles and not be binding.

2.5.8.2 MFSA Position

Board effectiveness can be enhanced through regular and well-structured board meetings. The Authority believes that holding regular board meetings, the timely circulation of board meeting materials and having board discussions appropriately minuted are good Governance practices.

In this light, the Authority will be retaining its proposals, but the relevant principle will be drafted in a general way covering the criteria mentioned as part of this proposal, but it will not be prescriptive in specifying certain matters (such as the frequency of board meetings etc.) Such element will then be covered in the supplementing Rules and/or guidance notes (as applicable).

2.5.9 Conflicts of Interest and Related Party Transactions

The Authority proposed [i] extending the scope of the existent rules on conflicts of interest; [ii] introducing a new obligation requiring the company secretary to maintain and periodically review a register of interests in addition to the existing obligation for directors to avoid and disclose any actual or potential conflicts of interest; [iii] laying down provisions vis-à-vis related party transactions; [iv] requiring entities to mitigate risks arising from these transactions and explain how they intend to do so.

2.5.9.1 Feedback Received

The majority of respondents agreed with the proposals put forward.

It was suggested that rather than the Company Secretary, it ought to be the compliance function which is involved in managing the disclosure of actual or potential conflict of interests and the maintenance of the register of interests given that conflicts of interest management are an element of a compliance officer's day to day work.

Furthermore, and specifically regarding the Register of interests, respondents recommended that this should be an internal document which is updated when a potential or actual conflict of interest arises. Clarity was sought on the retention period for such register and the frequency of reviews thereof.

The vast majority of respondents agreed with the approach suggested by the MFSA in relation to Related Party Transactions. Such respondents were also in favour of introducing a materiality threshold that would qualify a transaction as "relevant" and therefore subject to the requirement, as this was reflective of the proportionality principle. A respondent suggested that the materiality threshold should also take into account aggregate transactions that would be considered immaterial if analysed on a stand-alone basis.

This notwithstanding, there were some respondents who suggested that the materiality threshold should not be applied in the event of an actual conflict of interest. A respondent pointed out that in the interest of good Corporate Governance, all related party transactions, irrespective of their value, should be recorded.

Furthermore, it was also proposed that the threshold should be established by the entity itself, depending on, for instance, the nature of business, transactions and parties involved, in order to ensure that a one-size-fits-all approach is not adopted. Some respondents also sought clarity on who would be entrusted with a review and approval of such transactions, and it was proposed that, in virtue of its oversight role, the responsibility should be assigned to the Audit Committee.

Other respondents highlighted that related party transactions are extensively regulated by the existing regulatory framework, particularly with respect to listed companies, and it was therefore proposed that the Authority minimises regulatory overlaps by issuing rules that are consistent with existing provisions. It was also argued that extending the scope of related party transactions requirements to unlisted entities would result in adding an extra layer of prescriptive rules, leading to a disproportionate burden on SMEs.

2.5.9.2 MFSA Position

The Authority deems the disclosure of actual or potential conflict of interests essential to arrive at a balance between risk mitigation and economic outcomes.

The Authority is of the view that a core principle on disclosure of both potential and actual conflicts of interest merits inclusion within the new framework. Such principle shall cover the need for the board to take action to identify and manage and mitigate conflicts of interest and to ensure that the influence of third parties does not negatively impact the independent judgement of board members.

The Register of Interests is also considered crucial. The proposal will be retained, however, allowing flexibility in the implementation of the requirement, including in terms of who would be responsible for the maintenance of the register and for managing and overseeing the disclosure of conflicts of interest. As part of its supervisory process, the Authority may decide to require entities to provide additional details when deemed necessary.

With respect to Related Party Transactions, the Authority has noted that there appears to be an overall agreement on the proposal. It will therefore be retained within the new framework. The Authority will ensure consistency with the existing provisions within the Listing Rules and any other existing regulations.

Furthermore, with regard to the proposed 'materiality' threshold in relation to third party transactions, the Authority has considered the views provided in this respect and will not be introducing such measure in the principles.

2.5.10 Advisors of the Board

In order to ensure that crucial decisions are taken by the Board of Directors and not by other persons, the Authority proposed the introduction of a provision which ensures that advisors' roles are limited to advisory services and do not extend to decision-making.

2.5.10.1 Feedback Received

The feedback received indicated mixed positions regarding the role of professional advisors of the board.

Some respondents were supportive of the proposal stating that this would emphasize the responsibility of the board for its determinations and that this would further clarify that advisors only have a consulting role and are not furnished with decision-making powers. A considerable number of respondents were of the opinion that Directors should bear the responsibility of decisions taken when onboarding advisors' recommendations, highlighting that it was important for the directors to possess the necessary skill set to understand and challenge advisors.

Respondents highlighted that seeking proper professional advice should be encouraged where a decision may have a significant impact on the entity or the group. A respondent also recommended that advisors should, however, be allowed to flag any concerns they may have and that their recommendations should be documented in meeting minutes.

Amongst the respondents who were in disagreement, some argued that the Authority's proposal does not add any value to the Corporate Governance framework, suggesting that whilst this was indeed a good practice, it should not be included as a principle in the new framework being proposed. Furthermore, they are of the view that board members should be cognisant of their legal obligations and responsibilities, including their liability for decisions taken.

2.5.10.2 MFSA Position

The Authority is of the view that a clear separation between advisors/ 'shadow directors' and board members should be maintained.

In this respect, further to the feedback received, it was resolved that a provision ensuring that the role of advisors is limited to an advisory role and that it does not extend to decision-making will be introduced in rules/ guidance, rather than in the form of a principle.

The Authority will also provide for a provision that encourages boards to seek professional advice where there are issues that are significant for the entity. Any such advice should be recorded in board minutes.

2.5.11 Responsibilities of Functionaries and Officials

The Authority proposed the introduction of several provisions setting out the responsibilities of a number of officials such as: [i] the Chairman of the board and Chief Executive Officer; [ii] the Company Secretary; [iii] the Compliance Officer; and [iii] the Money Laundering Reporting Officer.

2.5.11.1 Feedback Received

Overall, the majority of respondents agreed with the proposal put forward by the Authority to clearly define the roles and responsibilities of the different officials, highlighting however that smaller entities should not be burdened with excessive requirements, in line with the principle of proportionality. Some respondents argued that the Corporate Governance Code should avoid reiterating provisions which replicate existent provisions. Moreover, some respondents submitted certain reservations as shall be outlined below.

1. Chairman of the Board and Chief Executive Officer

The discussion paper emphasises the segregation of the roles of the Chairman of the board from that of the CEO. Respondents are generally in agreement with the proposal, outlining that the separation of the two roles will enhance the board's independence from management, leading to better monitoring and oversight. Some respondents felt that proportionality should, however, play a key role in this respect. It was also recommended that the majority shareholder should not be able to be appointed as Chairman, in line with the principle that the board composition should ensure that no person or group of persons can dominate decision making. Whilst the majority of respondents agreed that the role and responsibilities of the Chairman and Chief Executive Officer should be clearly set out, some respondents expressed concerns with respect to the proposal of having the Chairman selected from one of the directors. It was stated that the independence of the Chairman would be affected by his previous role as director of the same entity. Moreover, respondents suggested that shareholders should retain the right to appoint a different individual which may bring a new direction to the strategy of the company, or where any of the current directors are considered suitable to be appointed as Chairman.

2. Company Secretary

With respect to the proposal of enhancing the role of the Company Secretary, some respondents stated that the role merits better visibility, since it is crucial for the proper functioning of the board. Others pointed out that the duties of the Company Secretary in Malta are determined by the Companies Act and it is therefore unnecessary to regulate such office through the Corporate Governance Code.

3. Compliance Officer

Respondents noted that specific reference to investment services is made within the Discussion Paper. They suggested that entities selling other products should also have been included, specifically those which target retail clients. Clarity was also sought in relation to the independence of the Compliance Officer for insurance undertakings in view of the provisions of Solvency II.

4. Money Laundering Reporting Officer

Respondents raised concerns about extending the requirement to appoint a MLRO to companies that are not required to appoint an MLRO under the relevant legal provisions. They felt that the inclusion of requirements related to AML/CFT in the Corporate Governance Code would increase the risk of having contradictory provisions.

2.5.11.2 MFSA Position

Having noted the issues and concerns being raised and in view of the feedback received, the MFSA will be taking a position as follows:

1. Chairman of the Board and Chief Executive Officer

The Authority shall be including a principle outlining that the roles of Chairman of the board and Chief Executive Officer should not be exercised by the same person. This is in line with the checks and balances associated with international Corporate Governance best practices.

However, the principle of proportionality will be taken into account with respect to the application of this principle. Accordingly, this principle will also include provisions in the Code on the implementation thereof together with supplementing Rules or guidance as necessary (depending on the type of entity/ authorisation held).

With respect to whether the Chairman should be selected from amongst the directors, the Authority will be applying the principle of proportionality in this respect as well, allowing entities to exercise their discretion.

The Authority decided to include such matter as part of the 'Effective Board' Principle.

2. **Company's Secretary**

The Authority has noted the feedback received and is reconsidering the inclusion of this principle.

3. Compliance Officer

In view of respondents' views, the Authority is considering adopting a holistic approach and has decided not to pursue the introduction of a principle defining the role and responsibilities of the Compliance Officer.

The Authority shall be including an overarching principle (under 'Internal Controls') outlining that the Board of Directors is responsible for setting up policies and procedures to identify and manage risks, for the oversight of the internal controls framework and for specifying the amount and type of risk the entity is willing to accept in order to achieve its strategic objectives.

4. Money Laundering Reporting Officer

Similarly, as indicated above for the Compliance Officer role, the Authority will not be including a reference in the principles to the role of MLRO, but rather a general principle covering internal controls. With regard to AML,

entities who are required to appoint an MLRO in terms of the applicable regulatory framework should ensure that it is only accepted by individuals who fully understand the extent of the responsibilities attached to the role.

When appointing an MLRO, a company must ensure compliance with all applicable AML, Sanctions and Anti-Bribery and Corruption Laws as well as any sector-specific Implementing Procedures issued by the FIAU in terms of the provisions of the Prevention of Money Laundering and Funding of Terrorism Regulations.

The Authority has considered carefully the feedback received with respect to the proposal that all entities, including those who are not subject persons shall appoint an MLRO and has decided not to introduce this measure.

2.6 Engagement with Stakeholders

In order to ensure that directors and key executives act responsibly and promote the success of the company for the benefit of all individuals or entities that may have an interest in it, the Authority had proposed the introduction of provisions to enhance engagement and dialogue with stakeholders. Stakeholders' views should affect the company's strategic decisions, and it was proposed that the new Corporate Governance Code would require Directors to explain how their views have been taken into consideration in the decision-making process.

2.6.1 Feedback Received

Respondents submitted mixed views on the proposal to enhance stakeholder engagement. Whilst some respondents agreed in principle, stating that stakeholder participation in strategic decisions is one of the key elements of good Governance, others were of the opinion that the Authority's proposal would be difficult to implement in practice.

It was pointed out that a provision requiring large entities to obtain the views of stakeholders for each decision would be unrealistic given the different types and the large number of stakeholders involved. Furthermore, it was claimed that the requirement may be unproportionally onerous for smaller firms.

A respondent also highlighted that, for listed entities, disclosures on how entities engage with their stakeholders could be commercially sensitive and may affect competition. Some respondents suggested that the Authority should further clarify its expectations on how the board is expected to engage with stakeholders and the extent of such disclosure.

2.6.2 MFSA Position

The Authority acknowledges the concerns submitted by respondents. However, the Authority believes that, given that an entity's success also depends on its relationship with groups of stakeholders and in order to ensure effective engagement with and encourage participation from entities' main stakeholders, provisions are to be included in the list of principles. The provision shall cover the need for the board to maintain an effective dialogue with such groups in the best interests of the entity.

Additionally, with regard to the proposal outlining the need for entities to disclose the manner of how they have engaged with stakeholders, the Authority has been decided not to introduce such provision.

In this respect, the Authority has also taken note of the need for a definition of 'stakeholders' and will also consider providing guidance on such definition.

2.7 Engagement with Shareholders

In order to enhance shareholders participation in the entities' strategy, the Authority is proposing reinforcing the existing framework by laying down provisions for the board to [i] regularly seek shareholders' feedback and constantly be aware of their views; [ii] develop a constructive dialogue with shareholders; [iii] ensure that all the necessary facilities and information are available for shareholders to be able to exercise their rights; and [iv] treat all shareholders equally, irrespective of their holding.

2.7.1 Feedback Received

Respondents put forward mixed views in relation to the Authority's proposals on shareholder engagement. On the one hand, a number of respondents agreed with the proposal. A respondent proposed limiting the application of the provision solely to those processes where key corporate decisions are taken. On the other hand, others expressed concern, stating that shareholders and minority rights are already protected at law, and the Authority's approach would be difficult to implement for entities that have a large number of shareholders.

Some respondents were of the opinion that shareholders should exercise their rights in general meetings where they can appoint Directors and Auditors and express their concerns and opinions. They expressed concern that the requirement for an entity to be constantly aware of shareholders' views is unrealistic and may slow down the decision-making process. Furthermore, it was also argued that this should not be applicable to private-owned authorised firms, where shareholders are directly represented at board level.

2.7.2 MFSA Position

The Authority has analysed the feedback received and shall be retaining the proposal set out in the Consultation Document, requiring entities to have in place procedures to ensure the proper exercising of the rights attributed to shareholders.

The Authority will put forward a core principle with a view to (i) safeguard the power of shareholders to influence corporate decision making; and (ii) ensure the equitable treatment of shareholders, including those in the minority. These principles will also include guidance on the implementation thereof.

2.8 Engagement with Institutional Investors

The Authority had proposed provisions aimed at promoting best practices and encouraging a proactive approach by institutional investors. Namely, the Authority proposed the introduction of a requirement to have policies with respect to the engagement therewith in place in order to increase institutional investors' engagement. It was proposed that such policies are to be made available to all shareholders and any conflicts of interest disclosed.

2.8.1 Feedback Received

There was a number of respondents who supported the introduction of a framework requiring mandatory policies and procedures in place in order to improve engagement with institutional investors while at the same time protecting the rights of minority shareholders. They outlined that the code should ensure the right balance between the increased engagement of large institutional investors and protection of the rights of small investors, granting, in all instances, the equal treatment of all shareholders.

Other respondents, however, stressed that this requirement typically applies to public companies with listed shares. Furthermore, some respondents considered that this requirement proposed by the Authority is unnecessary, as they considered themselves to already possess sufficient knowledge and expertise to effectively contribute to good Corporate Governance, also highlighting that extensive due diligence checks are carried out prior to and during any investment they undertake.

2.8.2 MFSA Position

The MFSA has noted the feedback received, and in view of the above, the MFSA will not be including such requirement in the list of principles.

2.9 Engagement with Employees

In order to protect individuals who expose improper practices such as misconduct and/or dishonest or illegal activity in their organisation, the MFSA proposed the introduction of a provision requiring entities to have adequate procedures in place to encourage this practice and to ensure proportionate and independent investigation of such matters.

2.9.1 Feedback Received

A number of respondents supported the proposal requiring entities to adopt formal policies to empower and encourage the workforce, as well as other stakeholders, to flag unethical behaviours of Directors and Senior Executives.

Some respondents, however, stated that they consider that the matter is already regulated under the Protection of the Whistle-blower Act, and certain entities are already subject to these requirements.

Representatives of listed entities pointed out that engagement with employees in the form of continuous training and informative sessions should be encouraged.

2.9.2 MFSA Position

In view of the above considerations and the feedback received, the MFSA believes that the personal and social wellbeing, safety, and security of the employees should be at the forefront of the companies' objectives while allowing them the space to take an active interest in the environmental, social and Governance philosophy of the company.

A provision will be included within the new framework as part of the 'Stakeholder Engagement' principle, ensuring that employees are able to raise any matter of concern.

2.10 Committees

The MFSA is considering introducing provisions relating to the appointment of [i] an Audit Committee, [ii] a Risk Committee, [iii] a Remuneration Committee, [iv] a Nomination Committee, and [v] a Good Governance Committee, all of which would be appointed by the board, based on the principle of proportionality. Such provisions would include details on composition, structure, the procedures to be followed and the contents of the charter of such committees. When appointed, committees should be listed on the entity's website and their work summarised in the annual report.

2.10.1 Feedback Received

Respondents were generally in agreement with the proposals put forward by the MFSA. This notwithstanding, some concerns were raised with certain respondents arguing that the introduction of several committees may lead to having fewer meetings in practice.

Several respondents suggested that provisions relating to committees should be high level principles emphasising proportionality as the setting up of multiple committees may be difficult to implement for SMEs. Respondents highlighted that, since the number of qualified individuals available locally is limited, this requirement may lead to the appointment of the same individuals on different committees, thereby defeating the whole purpose of having such committees in place as this would limit the value in terms of good Corporate Governance.

It was also recommended that, based on such considerations, committees composed of the same directors and/or discharging reasonably comparable roles could be amalgamated. Other respondents outlined that the MFSA's expectations should be made clear, seeking clarifications on whether some requirement/s may be carried out at the group level.

A group of respondents suggested that, rather than setting out prescriptive rules requiring every board to establish all the above-mentioned committees, the Authority should provide guidance on their expected functions, allowing discretion for the boards to determine how the ends are achieved, depending on size.

In relation to disclosure requirements, respondents requested the MFSA to clarify whether these should be carried out on the entity's website or else whether the annual report should suffice. A clarification should also be included on how firms without an institutional website would comply with the requirement. A respondent also outlined that publishing lists of committee members on company websites might be considered as an unnecessary distribution of personal data.

Specific feedback was also submitted in relation to the different committees, as summarised hereunder:

Audit Committee

Many respondents agreed that all companies should have an Audit Committee. A respondent also highlighted that separate and properly functioning Audit, and Remuneration Committees are essential.

Risk Committee and Remuneration Committee

It was suggested that SMEs should be exempt from the requirement and that the proportionality principle should apply.

Good Governance Committee

A respondent argued that the whole board is responsible for Governance arrangements and that this responsibility should not be delegated to just a few members but assumed in full by all directors.

Nomination Committee

It was suggested that a board succession policy should take into consideration the limited pool of resources available on the local market and the fact that, ultimately, the power to make appointments is vested in the shareholders, independently of the advice of the nomination committee. It was highlighted that the role of the nomination committee in the context of succession planning is generally quite limited and merely consultative.

2.10.2 MFSA Position

The MFSA sees merit in the feedback received from participants and noted the reservations raised, particularly that the establishment of certain committees for certain firms would be too burdensome and not proportionate to their size, nature, scale, and complexity. The Authority considers that given the applicability of this Code will be on a best effort basis, the issue of proportionality in relation to the establishment of Committees shall be adequately addressed. As specified earlier on, entities subject to mandatory Rules prescribing the establishment of certain Committees, those requirements will prevail.

The provisions to be included in the Code are expected to cover that where entities intend to or are otherwise required to appoint committees (in terms of the respective legislative and regulatory framework), the responsibilities of such committees should be clear, set out in writing, agreed by the Board of Directors and (where required in terms of the applicable legislative and regulatory framework), also made publicly available.

The Authority believes that the above decision should ensure that there is a sufficient level of flexibility for entities falling within the scope of the proposed new framework, as well as ensuring that there are no conflicts with existing legislation and regulatory frameworks.

2.11 Corporate Culture

The Authority is proposing the introduction of provisions setting out the responsibility of the Board of Directors to establish a culture which is aligned with the strategy of the entity, enhancing trust, integrity, and ethics,

preserving the long-term value of the enterprise, thereby creating a top-down approach to positive corporate culture.

2.11.1 Feedback Received

The majority of respondents supported the MFSA's proposal; however, it was submitted that corporate culture goes further than adherence to provisions in the regulatory framework, and it should therefore be up to each individual entity to understand the importance of setting the right culture and not including additional regulatory provisions. Some respondents suggested that these provisions should be stipulated in the form of recommendations rather than prescriptive provisions.

It was also noted that the core values of corporate culture are *de facto* established and maintained by the executives of the entity, who may not necessarily sit on the board. The new provisions on Corporate Culture should target not only directors but also individuals responsible for the day-to-day management of the company.

2.11.2 MFSA Position

The Authority is of the opinion that the proposal on Corporate Culture should be retained. A strong and accountable corporate culture is essential to generate value in the long term and to increase resilience. In this respect, it is considered crucial for the board to establish the right tone at the top and to set the standards which directors should follow to encourage good Governance throughout the organisation. The board should also assess and monitor culture, driving behaviours aligned with the company's strategies and values, preventing misconduct, and supporting the delivery of long-term success.

This notwithstanding, in the drafting on the related principle, the Authority will give due consideration will be given to proportionality, particularly in light of the diversity of firms that will be impacted by the new framework. Furthermore, such matter is expected to be included as part of the overall 'The Responsibilities of the Board' principle.

2.12 Ethics Framework

Further to the provisions on Corporate Culture, the Authority is also proposing that entities would have in place an Ethics Framework, which includes a code of ethics.

2.12.1 Feedback Received

Respondents were almost unanimously in agreement with this proposal. They suggested that any new rules in this respect should not be only applicable to decision makers within the entity but also to officials and employees. This would ensure that everyone is clear on the mission, values and guiding principles of the entity.

2.12.2 MFSA Position

Given the overall support of respondents, the Authority shall be retaining its position in this respect. Furthermore, in terms of Code structure, such matter is expected to be included as part of 'The Effective Board' principles.

2.13 Risk Management

The Authority had proposed introducing provisions vis-à-vis Risk Governance and expected controls in order to reinforce the risk management and controls within entities.

2.13.1 Feedback Received

The majority of respondents agreed with this proposal sharing the view that the board is entrusted with the role of monitoring risk indicators and establishing the risk appetite of the company.

Many respondents stated that the risk management framework should be implemented in accordance with the proportionality principle given that entities that differ in size, structure and business model have different risk exposures, and the role of the risk management function should be considered as being more important in some entities than in others.

It was recommended that for SMEs not subject to regulatory requirements in this respect, these provisions should be introduced as a best practice and not as a requirement *per se*.

Certain respondents suggested including these provisions within the respective regulatory frameworks rather than in the new Corporate Governance Code. Others suggested that the Authority should introduce provisions to enhance the importance of having board members who possess technical knowledge and experience in risk management.

Furthermore, several respondents asked for clarity on: [i] whether the board would be obliged to appoint amongst themselves a director, who is specifically entrusted with the oversight of the entity's risk management function; [ii] whether the entity would be expected to formulate and adopt a risk register, including minimum requirements to be included therein; [iii] the content of the policies and procedures that the entity would be expected to have in place.

2.13.2 MFSA Position

The Authority believes that risk management is a crucial element to *inter alia* enhance the resilience of entities in the longer term, especially where such entities are exposed to unexpected circumstances. The COVID crisis has further highlighted the importance of good risk management practices in order to mitigate, manage and control the impact of unexpected risks.

In light of these considerations and responses received, the Authority is retaining the proposal discussed in the Consultation Paper, based on the principle that the Board of Directors is responsible for risk management,

setting the risk appetite and assessing and monitoring the entity's main risks and procedures, which must be kept up to date.

However, it intends to amend the principle to make reference to 'Internal Controls', also to cover internal and external Audit, as well as oversight of internal controls of the entity. Besides the key risk management element, this principle will accordingly be highlighting the need for entities to establish transparent policies and procedures to ensure that an effective internal and external audit function is in place, as well as exercising oversight of the entire internal control framework.

The Authority also noted the requests for further clarity submitted by some respondents in this regard. These will be provided at a later stage, in upcoming consultation exercises on the subject matter at hand.

2.14 Anti-Money Laundering and Combatting the Funding of Terrorism

In order to enhance robust Governance, effective processes, and adequate and effective systems and controls to manage their ML and FT risk, the Authority proposed the introduction of a provision within the Code specifically on AML/CFT.

2.14.1 Feedback Received

Respondents provided mixed feedback. Whilst some respondents agreed with the proposal to have robust Governance, effective processes, and adequate internal control mechanisms to manage ML and FT risks, others submitted that the provision should not apply to companies that do not fall within the scope of the AML regulation. It was also argued that since different sectors have different exposure to ML/FT risks, the proposed requirements would need to be sector specific and proportional.

Some respondents also recommended that matters retaining to AML/CFT should be retained within the applicable AML/CFT laws, regulations and the Implementing Procedures issued by the FIAU, in order to avoid any discrepancy or confusion. Having the Corporate Governance Framework replicating such provisions was deemed unnecessary.

2.14.2 MFSA Position

The Authority has taken note of the feedback received, and in order to avoid duplication of provisions emanating from the various frameworks and ensure consistency, it intends to include reference to the AML/CFT related controls as part of the 'Internal Controls' principle.

2.15 Continuous Professional Development

Given the constantly evolving regulatory environment, the MFSA is proposing the introduction of a Continuous Professional Development requirement for Directors, including a requirement for a number of mandatory CPD hours to ensure that the knowledge and skills of Directors are up to date.

2.15.1 Feedback Received

Mixed feedback was received in this respect. Whilst some respondents were of the opinion that directors should be expected to keep abreast with developments in the course of their duties as part of their mandate, others argued that a minimum number of mandatory CPD hours should not be imposed as this should be left entirely at the directors' discretion.

Respondents also suggested that: [i] the number of CPD hours to be maintained should be based on a three-year rolling period; [ii] the Authority should organise annual seminars for directors in order to contribute to their professional development; and [iii] specialised, topic-based, tailored training should be made available to Directors, and favoured over general CPD.

Clarification was also sought on: [i] which areas of professional development would be considered relevant for CPD; and [ii] which organisation/s would be certified to provide said training.

2.15.2 MFSA Position

The MFSA is of the view that it should continue fostering an environment wherein the governing body is required to have adequate professional skills and knowledge to effectively perform its duties. The Authority is committed to ensuring that members of the governing body regularly update and refresh their knowledge on regulatory developments and best practices.

In view of the above considerations and the feedback received and also given the related administrative implications relating to the implementation and administration of a prescriptive CPD framework, the MFSA is of the view that the requirement of a formal CPD framework matter merits further consideration and discussion. This aspect is accordingly intended to be treated in greater detail at a future date.

However, whilst a prescriptive CPD framework will not be introduced at this stage, the Authority will be including provision for the board to ensure adequate ongoing training and development (besides possessing appropriate qualifications and experience, commensurate to their role and the type of entity in relation to which they are being appointed), within the 'Structure and Composition of the Board' principle.

Further to the above, it is also to be noted that as part of the overall efforts to strengthen Governance standards, as part of future policy work, the Authority may also consider introducing prescriptive qualifications and/or years of experience needed for the governing body members occupying roles on certain types of regulated entities.

2.16 Professional Indemnity Insurance

Given that directors and key functionaries may be considered personal or jointly liable, under the Companies Act, the Authority is proposing including a provision stating that directors shall take out professional indemnity cover.

2.16.1 Feedback Received

The majority of respondents expressed concerns in this respect. Several respondents submitted that the board should be covered by a Directors and Officers Liability Policy rather than a Professional Indemnity policy. The D&O Liability Policy would serve the aim to protect directors and officers when personal liability may arise.

It was also recommended that it should be left up to the entity whether to provide such cover on the basis of an internal assessment in order to avoid excessive risk taking. Other respondents believed that due consideration should be given to the proportionality principle, exempting some entities from this requirement.

2.16.2 MFSA Position

Following feedback received by respondents and further considerations on the matter, the Authority has revised its proposal. The Authority is of the view that considering that Directors are expected to fulfil their obligations to a high standard, taking out professional indemnity cover for claims made against them (such as for acts of omission or recklessness) may potentially discourage them from acting up to the standard, as expected by the Authority.

Given these considerations and the feedback received, the Authority has decided not to pursue the introduction of a professional indemnity cover. The Authority is, however, considering having such matter covered in the form of Guidance Notes supplementing the various regulatory frameworks.

2.17 Business Continuity and Disaster Recovery

In order to ensure business continuity and minimise losses, the Authority had proposed the introduction of provisions requiring companies to have strategic management processes, which identify potential threats, and which fully consider disaster recovery and business continuity.

2.17.1 Feedback Received

The proposal was well-received by the majority of respondents stating that it would enhance the application of the principle of sound and prudent management. It was also noted that this requirement was already reflected in a number of financial services regulations, with one respondent suggesting the inclusion of enhanced provisions in the existing regulatory frameworks rather than including separate provisions in the Corporate Governance Code.

It was also recommended that the Authority should issue guidance regarding [i] the expected minimum contents of such plans; [ii] requirements for entities that have solely business-to-business relationships; and [iii] requirements for those entities whose main stakeholders will be individual customers.

2.17.2 MFSA Position

The Authority will be maintaining its position in this respect. COVID has further exacerbated the requirement to have in place robust business continuity and disaster recovery arrangements, which aim to minimise losses and

ensure continuity of critical business functions. Identifying key risks and having the necessary procedures in place to ensure continuity in the event of disruption are considered essential.

2.18 Disclosure

In order to strengthen the requirements around transparency, the Authority had proposed introducing a provision which will require authorised and listed entities to disclose both financial and non-financial information, including *inter alia* statements related to sustainable finance and corporate social responsibility.

2.18.1 Feedback Received

The Authority has received mixed reactions in relation to this proposal. Respondents in favour highlighted that non-financial reporting should be enhanced in Annual Reports and agreed on sustainable finance disclosures.

Those respondents in disagreement submitted that the Directors' report already includes such non-financial information. The argument that sectoral legislation already includes several disclosure requirements, and that duplication of requirements should be avoided was once again raised.

A respondent also suggested that the Authority should consider taking a proportionate approach in relation to disclosure obligations in order to avoid excessive burden on SMEs.

2.18.2 MFSA Position

The Authority believes that further steps should be taken to enhance the quality of Governance disclosures for the benefit of all stakeholders.

The Authority also notes the ongoing [European Commission's sustainable Corporate Governance initiative for 2021](#), as well other EU regulatory developments covering disclosure requirements. In this regard, in view of these developments, whilst the Authority intends to include a core principle focusing on 'corporate sustainability', it intends to consider the focus of this principle further. This is in order to both ensure alignment with the aforementioned regulatory developments, as well avoid duplication with the current applicable required reporting requirements emanating from the various frameworks. Further guidance shall be provided in this respect.

In this regard, further to feedback received and in order to avoid duplication, the Authority intends to integrate the proposed 'Disclosure' principle as part of the 'corporate sustainability' and 'corporate social responsibility' principles (listed in Section 3.4 of the proposed List of Principles as presented in Part 3 hereunder).

2.19 Compliance Statement

The Authority is considering introducing a requirement to publish a statement vis-à-vis compliance with the Corporate Governance framework, which will identify areas of material non-compliance with the Code and give reasons, where applicable, for any alternative practices adopted. It was also proposed that a statement should be drawn up by the company's auditors.

2.19.1 Feedback Received

Many respondents welcomed this proposal, highlighting that entities which do not comply with Governance requirements negatively impacted the overall industry's reputation. That stated, respondents recommended that requirements which are already found in existing sectoral regulatory frameworks are not regulated in order to avoid duplication and/or conflicts.

On the other hand, some respondents pointed out that the requirement to publish such a statement in the annual report would have significant cost implications for small entities and that this may, in some cases, outweigh the benefits. This was particularly emphasised with respect to the proposal relating to the statement, which is to be drawn up by the company's auditors.

A respondent argued that a mandatory declaration in this regard is not consistent with a principles-based approach.

Specifically, in relation to the proposal on requiring entities to publish their compliance statement on their website, some respondents sought clarification on how this would apply in practice, particularly where the company is part of a group. A respondent also suggested that the compliance statement should be submitted only to the MFSA.

2.19.2 MFSA Position

In view of the change in position and proposed revision in the type of Code, this requirement is no longer applicable.

2.20 Corporate Social Responsibility

The Authority proposed reinforcing the Corporate Social Responsibility principle within the Maltese Corporate Governance framework. A provision to ensure that "*organisations disclose policies and performance relating to business ethics, the environment and, where material to the company, social issues, human rights and other public policy commitments*" was proposed.

2.20.1 Feedback Received

The majority of respondents agreed in principle with the Authority's proposal. They highlighted that Corporate Social Responsibility is a crucial matter and authorised entities as well as listed entities as it ultimately ensures that business is conducted in an ethical manner.

This notwithstanding, some concerns were raised. Respondents noted that requiring SMEs to disclose Corporate Social Responsibility activities may create competitive disadvantages. It was, therefore, suggested that these provisions should be drafted in a generic manner to ensure that all entities would be captured, but with certain requirements being made applicable only to large entities.

Other respondents suggested that provisions in relation to CSR should be applied on a voluntary basis. A respondent also suggested that the importance of the concept of Environmental Social Governance (ESG) should be stressed.

2.20.2 MFSA Position

Whilst noting the responses received, a principle urging firms to disclose policies in relation to the business ethics, the environment and where material, to the company, social issues, human rights and other public policy commitments, will be introduced within the new framework.

3 Way Forward: MFSA Code on Corporate Governance

As stated in section 2.4 of this Feedback Statement, the Authority intends to proceed to issue a list of main principles in the form of a List of Principles. The main principles will be supplemented by supporting provisions, acting as guidance for achieving the main principles.

The framework (consisting of main principles and supporting provisions) will be applicable on a 'best effort basis'. These principles will also be supported by sector-specific complementing Guidance Notes and/ or updates to the Governance section of the MFSA Rulebooks (as applicable) and/or sectoral Codes. In determining whether any of the requirements are to be included in the relevant Rulebooks or else by guidance notes or Codes, the Authority will take note of various criteria, including the existing provisions included in the various frameworks and the risk classification of these entities as determined by the MFSA.

Whilst the Authority's policy work relating to the Code on Corporate Governance is yet to commence, the MFSA is hereby providing the industry with an indicative outline of the proposed structure for the MFSA Code on Corporate Governance:

- 1 Scope and application of the Code
- 2 Definitions
- 3 Principles of Good Corporate Governance
 - 3.1 The Effective Board
 - 3.1.1 Structure and Composition of the Board
 - 3.1.2 Appointment and Succession
 - 3.1.3 The Responsibilities of the Board
 - 3.1.4 Chairman of the Board and Chief Executive Officer
 - 3.1.5 Remuneration
 - 3.1.6 Evaluation of the Board's Performance
 - 3.1.7 Board Meetings
 - 3.1.8 Conflicts of Interest and Confidentiality
 - 3.1.9 Ethics Framework
 - 3.2 Shareholders and other Stakeholders Engagement
 - 3.2.1 Shareholders Engagement
 - 3.2.2 Stakeholders Engagement
 - 3.3 Internal Controls
 - 3.4 Other principles
 - 3.4.1 Business Continuity and Disaster Recovery
 - 3.4.2 Corporate Sustainability
 - 3.4.3 Corporate Social Responsibility

In line with the commitment of the Authority to enhance engagement with its stakeholders, the Code of Principles may, in due course, be the subject of another industry consultation exercise. This would allow stakeholders to comment, make suggestions and submit contributions to the draft Code.

We also intend to strengthen our engagement with the industry through other channels. Such initiatives shall include, amongst others, the delivery of training sessions, thematic reviews undertaken by the Authority focused on Corporate Governance by Supervisory Functions, as well as providing updates on regulatory developments in this area. Such engagement will be focused to drive change in the culture of entities authorised by the MFSA, making also sure that the industry will be fully committed to implementing the highest standards of Corporate Governance.

Any comments or queries in relation to this Feedback Statement should be directed to CorporateGovernance@mfsa.mt.