



Guernsey Financial
Services Commission

FINANCE SECTOR

CODE OF CORPORATE GOVERNANCE

CONSULTATION PAPER

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INTRODUCTION

The purpose of the GFSC Finance Sector Code of Corporate Governance (“the Code”) is to provide Boards and directors of locally regulated financial services businesses with a framework for best practice of company governance.

The economic and financial crisis, which came to a head in 2008-2009, triggered widespread reappraisal locally and internationally, of the effectiveness of systems of governance. In addition, the needs for transparency, accountability and probity in modern and open societies have put new demands on business leaders. Business successes have shown that good governance can contribute to wealth creation, while weak governance can contribute to significant losses or corporate failures.

The intention of this Code is therefore to assist the local finance industry in encouraging the use of sound systems of governance, in order to maximise company performance and support value creation.

What is the GFSC Finance Sector Code of Corporate Governance?

The Code has been drafted to provide guidance on sound corporate governance for the regulated finance sector in the Bailiwick of Guernsey and seeks to influence the way in which directors carry out their responsibilities.

The Code provides a set of “Principles” and “Guidance”, but is not intended to be prescriptive; rather it is a formal expression of the components of good corporate practice, against which shareholders and Boards themselves can better assess the degree of governance exercised over companies in Guernsey’s finance sector. A failure to comply with the Code does not automatically make a company subject to it liable to any sanction or proceedings, but the GFSC will take into account the way in which and the extent to which companies have adopted the Code in their policies, procedures, controls and practices

It should be noted that the Code does not in any way reduce or otherwise change the obligations or enforceability of any enactment or other document.

Each business’s approach to corporate governance should reflect its legal and operating structure, as well as the nature, scale and complexity of the business. It is not suggested that ‘one size fits all’. The Commission recognises that the differing nature, scale and complexity of businesses will lead to different approaches to meeting the Code. Corporate governance will continue to evolve internationally and therefore the Code will require review and updating from time to time.

The Code’s function is to help boards discharge their duties efficiently and effectively.

Ultimately, corporate governance is about the behaviour of Boards and their directors.

Who is covered by the Code?

The Code provides a framework which applies generally to all companies who hold a licence from the GFSC under the regulatory laws. The regulatory laws are:

- (a) the Protection of Investors (Bailiwick of Guernsey) Law, 1987;
- (b) the Banking Supervision (Bailiwick of Guernsey) Law, 1994;
- (c) the Regulation of Fiduciaries, Administration Businesses and Company Directors, etc. (Bailiwick of Guernsey) Law, 2000;
- (d) the Insurance Business (Bailiwick of Guernsey) Law, 2002 (as explained below, companies licensed under this law, which are also subject to the GFSC's Licensed Insurers' Corporate Governance Code, are deemed to meet the GFSC's Finance Sector Code of Corporate Governance);
- (e) the Insurance Managers and Insurance Intermediaries (Bailiwick of Guernsey) Law, 2002.

Companies subject to the GFSC's Licensed Insurers' Corporate Governance Code are deemed to meet this Code.

References in this Code to "the Board", "Boards" or "Boards of directors" should be read as also meaning partners of a partnership, where the entity covered by the Code is not a company. Therefore, where the entity is not incorporated as a company and there are no directors appointed to oversee the business, partners have the same duties for any actions expected by Boards and directors under the Code.

The Code is not intended in any way to codify or amend existing laws or to confer rights which conflict with or add to rights arising at law. In the event of any incompatibility with existing law, guidance contained in this Code will be disapplied and law will prevail to the extent of any incompatibilities.

How does the Code work?

The Code is provided as guidance and is structured around a set of **8 Principles** and additional best practice **Guidance**:

- **Level one** – represents **Principles** of good corporate governance and sets out expected standards for Boards. The principles are included in bold type in blue boxes.
- **Level two** – provides further **Guidance** on best practice.

There are a number of reasons why this approach is considered to be appropriate for the sort of issues the Code seeks to address. These are:

- It recognises the differing nature and requirements of the individual financial services industry sectors operating in the Bailiwick;
- It accepts that the approach to corporate governance by companies needs to be proportionate and appropriate to the nature, scale and complexity of the business;
- It encourages companies to determine good practice, while recognising that there can be differing approaches to meeting the Code achieve good governance;
- It enables the Code to be more easily adapted to account for developments in best practice.

When does the Code become effective?

The GFSC aims to issue the Code in final form as early as possible in 2011.

The Code will come into effect on 1 January 2012 and the Corporate Governance Assurance Statement outlined in Section 6.2 of the Code should be included in companies' annual financial statements for financial reporting periods commencing on or after 1 January 2012. From 1 January 2012 companies will need to be in a position to discuss their governance practices with the GFSC.

It is anticipated that on 1 January 2012 the GFSC will withdraw its existing document "Guidance on Corporate Governance in the Finance Sector", which was issued in December 2004.

Consultation

In light of the material changes made to the initial draft Code as a result of the industry consultation process, it has been determined that a further consultation should take place on this revised document.

Interested parties who wish to make comments on levels one and two of the Code should respond in writing to this consultation paper by writing to the Policy and International Affairs Division of the GFSC by the close of business on 1 June.

Code of Corporate Governance

PRINCIPLES AND GUIDANCE

PRINCIPLE 1. THE BOARD

Companies should be headed by an effective Board of directors (“the Board”) which is responsible for governance .

1.1 *Governance structure*

The Board should have a clear governance structure which reflects the demands and complexities of the company’s business environment, strategy, company values, standards, risk appetite, internal controls and key policies.

1.2 *Central role of the Chairman*

The role of the Chairman is central to the effective leadership and corporate governance of the company. A Chairman should be elected for each meeting of the Board where there is no standing Chairman.

1.3 *Balance and composition of the Board*

The Board should comprise an appropriate balance of skills, knowledge and competence, taking into account its members’ relevant experience, such that the Board as a whole is able to discharge its duties and responsibilities effectively and that no individual or group of individuals can or does unduly dominate the Board’s decision making.

Taking into account the size, nature and complexity of the company, the Board may include one or more non-executive directors, including independent non-executive directors, in order to fulfil the requirement for an appropriate balance of skills.

1.4 *Committees of the Board*

The Board may, but is not obliged to, establish committees to analyse and review specific issues or to carry out functions, and provide advice and recommendations to the Board on them. While the Board may delegate powers and authority to committees, the Board will retain ultimate responsibility for the actions of committees, with such committees being under an obligation to report back to the Board. Each committee so formed should maintain clearly documented terms of reference.

1.5 *Delegation to management*

The Board should ensure that a clear and sufficient senior management structure is in place and should determine the powers and duties entrusted to management to enable them to perform their duties effectively. Such delegation does not absolve the Board from overall responsibility for the sound governance of the company.

1.6 *Board meetings*

The Board should meet sufficiently often to ensure that it fully discharges its duties in an effective manner.

PRINCIPLE 2. DIRECTORS

Directors should take collective responsibility for endeavouring to maximise the success of the company in directing and supervising the affairs of the business .

2.1 *Directors' duties*

Directors have a duty to operate in accordance with all relevant legislation and should also operate to a clear framework of specified responsibilities and reserved powers of the Board, suitable for the particular company.

2.2 *Legislation and regulation*

Directors have a duty to be conversant with applicable legislation, regulation, policy, rules, instructions, guidance and codes of practice to an appropriate level to enable them to discharge their responsibilities.

2.3 *Strategy*

Directors should take responsibility for company strategy and key policies.

2.4 *Appointment, induction and re-appointment of directors*

There should be a procedure for scrutinising nominations for the appointment of new directors to the Board and a suitable induction programme provided to new appointees. The Board should also satisfy itself that plans are in place for the orderly succession of its members.

2.5 *Commitment*

Prospective directors should confirm to the Board that they have sufficient understanding and time available to discharge their duties effectively, taking into account the number and importance of their other commitments.

2.6 *Provision of information and support for the Board*

The Board should be supplied in a timely manner with information in a form and of a quality appropriate to enable it to discharge its duties, facilitate decision making and allow for effective monitoring and control of company performance.

2.7 *Performance evaluation*

The Board should regularly evaluate the performance of its members and of the effectiveness of its actions.

2.8 *Training and development*

All directors should regularly update and refresh their skills and knowledge.

PRINCIPLE 3. BUSINESS CONDUCT AND ETHICS

All directors should maintain good standards of business conduct, integrity and ethical behaviour and should operate with due care and diligence and at all times act honestly and openly.

3.1 Conflicts, *policy and standards*

Boards should establish, implement and maintain an effective conflicts of interest policy which sets out standards of expected behaviour.

3.2 *Conflicts of interest*

Directors have a duty to avoid, manage or minimise conflicts of interest and should, wherever possible, arrange their personal and business affairs so as to avoid direct and indirect conflicts of interest. Any actual or potential conflicts of interest should be declared to the Board in accordance with legislation and dealt with in accordance with the company's memorandum and/or articles of incorporation or other constitutional documents, or by the other directors as they consider appropriate.

3.3 *Self dealing*

Any transactions between the company and its Board members should take place at arms' length or be disclosed in detail at a Board meeting before the Board considers the transaction. Any conflicted directors should consider abstaining from participating in the decision.

3.4 *Duty to the company*

Directors have a duty to act in the best interests of the company in fulfilling their fiduciary duties, taking into account the interests of their shareholders and customers.

Proposed Additional Wording for Banks

The board of a regulated banking subsidiary should retain and set its own corporate governance responsibilities, and should evaluate any group-level decisions or practices to ensure that they do not put the regulated subsidiary in breach of applicable legal or regulatory provisions or prudential rules. The board of the regulated banking subsidiary should also ensure that such decisions or practices are not detrimental to:

- the sound and prudent management of the subsidiary;*
- the financial health of the subsidiary; or*
- the legal interests of the subsidiary's stakeholders.*

PRINCIPLE 4. ACCOUNTABILITY

The Board should have formal and transparent arrangements in place for presenting a balanced and understandable assessment of the company's position and prospects and for considering how they apply financial reporting and internal control principles.

4.1 Strategic business management

The Board is responsible for the company's objectives and business plan.

4.2 Group policies

The Board of a company which is a member of a group should review any group policies and assess their relevance and applicability to the business and the legal and regulatory environment in which the company operates.

4.3 Financial reporting

The Board is responsible for the integrity of the company's financial statements and any other formal information relating to its financial performance, as well as any other statutory information required.

4.4 Internal control systems

The company should maintain a sound system of internal control to safeguard the company's assets and to manage risk, and the Board should regularly review such controls.

4.5 Audit and auditors

The Board should establish formal and transparent arrangements for considering how they apply financial reporting principles and for maintaining an appropriate relationship with the company auditors.

4.6 Performance monitoring

The Board should determine and ensure that relevant monitoring criteria of the company's performance are in place and should regularly evaluate their effectiveness.

4.7 Outsourcing functions

The Board should establish, oversee and retain responsibility for clear accountability for all material outsourced functions, as if these functions were performed internally.

4.8 Annual business reviews

The Board should, at least annually, undertake a review of the company's business activities and future prospects. Such reviews should be conducted to the extent appropriate to the current and proposed activities of the company.

PRINCIPLE 5. RISK MANAGEMENT

The Board should provide suitable oversight of risk management, establish a clear risk management strategy and maintain a sound system of risk measurement and control over all key risks.

5.1 Responsibility for risk

The Board should maintain overall responsibility for the risk management of the company and, where appropriate, should support and be supported by a senior executive of the company who has responsibility for assessing and managing risk.

5.2 Risk strategy and policy

The Board should determine the company's risk appetite and tolerance and developing policies, procedures and controls for identifying, evaluating and managing all significant risks faced by the company.

5.3 Risk reviews

The Board should undertake, at least annually, a review of the effectiveness of the company's risk management, and related policies, procedures and controls.

5.4 Contingency planning and testing

Companies should have in place properly constructed business continuity and contingency plans to safeguard against disruption of their operations and services and to mitigate risk. The Board should review these plans at least annually.

PRINCIPLE 6. DISCLOSURE AND REPORTING

The Board should ensure the timely and balanced disclosure to shareholders and/or to regulators of all material matters concerning the company.

6.1 Statutory disclosure and regulatory reporting

The Board has a duty to ensure that information is made available as required by applicable rules, regulations and codes and that all statutory and regulatory reporting deadlines are met.

6.2 Corporate governance reporting

The Board should include a Corporate Governance Assurance Statement in the Directors' Report in the annual financial statements of the company confirming that the directors have considered the effectiveness of their

corporate governance practices and are satisfied with their degree of compliance with the Principles set out in this Code, or alternative codes accepted by the GFSC, in the context of the nature, scale and complexity of the business.

6.3 Annual general meetings

Where the company is required to hold an annual general meeting, the Board, where required by shareholders, should use the annual general meeting to communicate with shareholders about relevant matters.

PRINCIPLE 7. REMUNERATION

The Board should ensure remuneration arrangements are structured fairly and responsibly and that remuneration policies are consistent with effective risk management.

7.1 Remuneration policy

The Board should review and set company remuneration policies. Such policies should, wherever possible, have regard for company and individual performance, and should avoid creating incentives that encourage excessive risk taking.

7.2 Levels of remuneration

Levels of remuneration should be sufficient to attract, retain and motivate individuals of the quality required to manage and run the company successfully. Additionally, remuneration of non-executive directors should reflect the time commitment and responsibilities of the role.

PRINCIPLE 8. SHAREHOLDER RELATIONS

The Board should ensure that sufficient communication takes place with shareholders and is based on a mutual understanding of needs, objectives and concerns.

8.1 Shareholder engagement

The company should have in place an appropriate communications strategy with shareholders and, where relevant, other third parties.

8.2 Rights of shareholders

The Board should respect the rights of shareholders, and ensure that facilities are made available for them to exercise their rights.

8.3 Shareholder profiles

The Board should regularly consider the shareholder profiles of the company and, where appropriate, have in place methods for obtaining and understanding the views of shareholders.

8.4 Shareholder responsibilities

The Board should encourage shareholders to make considered use of their votes and views and to engage appropriately with the Board.