



Financial Services Commission Mauritius

FSC\P\CL010705

By email

22 July 2005

CIRCULAR LETTER-CL010705

**To Directors
Management Companies and
Licensed Non-Bank Financial Institutions**

Dear Sir/Madam

NATIONAL CODE OF CORPORATE GOVERNANCE

Purpose of the Circular Letter

The National Committee on Corporate Governance has in accordance with section 65(c) of the Financial Reporting Act 2004 issued the Code of Corporate Governance –which has been published for general information in the Government Gazette (GN No. 844 of 2005) in May 2005. Pursuant to clause 1.1(b), the Code applies to all non-bank financial institutions. The purpose of this circular letter is to remind all licensees of their obligations arising under the Code which is effective as from the reporting year (financial period) ending 30 June 2005.

Who the Code applies to

The Code applies to all non-bank financial institutions who must comply with all provisions of the Code (clause 1.1(b) of the Code refers). This circular letter is addressed to all companies providing financial services licensed under the Financial Services Development Act 2001 (FSD Act), the Stock Exchange Act and the Insurance Act. These include, Management Companies, companies licensed under section 14 of the FSD Act, insurance companies and stockbroking companies. The Code will not apply to companies holding a Category 1 or a Category 2 Global Business Licence except those Category 1 Global Business Companies which provide financial services or which are involved in handling funds belonging to third parties, such as insurance companies and collective investment schemes.

Relevant provisions of the Code

The Code is divided into nine sections which cut across three main themes: governance structure, internal governance mechanisms, and reporting and disclosure.

Governance Structure

The board of directors or the governing body is the main player in the governance structure of a company and is ultimately accountable and responsible for the performance and affairs of the



company. Section 2 of the Code contains specific provisions regarding the structure, composition, and role and functions of the board that companies must comply with.

The Code sees a single or unitary board structure composed of executive, non-executive and independent directors as best capable of leading and controlling a company. The board may however form committees to perform defined tasks, namely, audit, risk management, corporate governance, remuneration or nomination committees. The Code lays down a number of principles with respect to the composition and membership of these committees. Where such committees are set up the board should stipulate their terms of reference, life span, role and function. The committees, in turn, report to the board on their activities and findings. The overall responsibility for the delegated duties remains, however, with the board.

The Code also prescribes best practices concerning the composition of the board and the suitability of board members. The board should endeavour to have an appropriate balance of executive, non-executive and independent directors who must be *“individuals of integrity who can bring a blend of knowledge, skills objectivity, experience and commitment to the board”*. Further, it recommends the separation of the title, role and functions of the chairperson of the board and of the chief executive officer. The primary function of the chairperson is to preside over meetings of directors and to ensure the smooth functioning of the board in the interests of good governance. The Code also lays down the important functions of the chief executive officer and the role of the executive, non-executive and independent non-executive director and that of the company secretary.

Section 2 of the Code sets out other principles which cover conflicts of interests, remuneration of directors, director selection, training and development and board and director appraisal.

Internal Governance Mechanisms

Companies are expected to have a system of risk management, an internal control mechanism and an internal audit function. It is the responsibility of the board to ensure that the company develops and executes a comprehensive and robust system of risk management. The board is also responsible for the system of internal control and must set appropriate policies to provide reasonable assurance that the control objectives are attained. The internal audit function aims at providing assurance to the board with regard to the implementation, operation and effectiveness of internal control and risk management. The board may delegate responsibility for managing the internal audit function and for receiving internal audit reports to the audit committee. However, where the board decides not to establish an internal audit function, it must disclose the fact in its annual report and state the reasons for its decision. The annual report must also contain an explanation as how in the absence of an internal audit function effective internal controls, processes and systems will be ascertained.

Reporting and Disclosure

Directors must keep adequate accounting records and prepare accounts which fairly present the state of affairs of the company and the results of its operations and which comply with International Financial Reporting Standards. External auditing is important for ensuring integrity in financial reporting. Good governance requires structures that promote the external



auditors' independence from the board. The audit committee plays a fundamental role in selecting and recommending to the board and shareholders the appointment of auditors.

The Code has adopted the inclusive approach which calls for a clear definition of the purpose of the company and the identification of its stakeholders. The values by which the company will carry on its daily affairs should be identified and communicated to such stakeholders. These three factors should be combined in developing the strategies to achieve the company's goals. The relationship between the company and its stakeholders should be mutually beneficial. Accordingly, companies are required to disclose information on a clear and timely basis. Having in mind the principle of transparency, boards are expected to address to shareholders and other stakeholders on matters of material interests. The annual report which is submitted under the Companies Act 2001 should realistically provide a comprehensive and objective assessment of the activities of the company so that all stakeholders can obtain a full and fair view of its performance.

The Code also recommends that companies report to its stakeholders on its policies and practices as regards ethics, environment, health and safety and social issues.

The implications of the provisions

How to report

The approach for monitoring compliance with the Code depends heavily on disclosure of corporate governance practices by companies. The Code requires companies to state in their annual reports the extent of their compliance with the Code. Clause 8.4 of the Code provides a non-exhaustive list of items which should be disclosed in the corporate governance section in the annual report. The annual report must also disclose areas of non-compliance and must state the reasons for non-compliance and the alternative practices adopted (if any) or measures that are being taken to ensure compliance. The board may request the auditors to assess and state the extent of the company's compliance with the Code.

What is expected of licensed NBFIs

All licensed NBFIs must comply with the Code and report on its compliance status in the annual report as from the reporting year (financial period) ending 30 June 2005. All annual reports filed with the FSC as from the financial year ending 30 June 2005 must contain a section on corporate governance pursuant to clause 1.6 of the Code. Where a licensee has a particular difficulty in complying with any aspect of the Code or any parts thereof, or where it has failed to comply in any particular respect, it should proactively advise the FSC and should state the reasons for the difficulty or failure in complying. The licensee must also indicate the alternative practices adopted (if any) or any measures that are being taken to ensure compliance.

Role of the FSC

Clause 1.8 of the Code provides that regulators are responsible for monitoring the application by these companies of the principles set out in the Code. The extent to which a licensee is able



to demonstrate compliance with the Code will be considered by FSC in the supervision of licensees. Failure to comply with the Code will not constitute a criminal offence. However, where circumstances so warrant, the FSC may direct a licensee under section 7(1)(d) of the Financial Services Development Act 2001 to comply with the Code or any part thereof.

Looking ahead

Having regard to the distinct risks and responsibilities of the insurance entities, the securities industry, corporate service providers and other NBFIs, the FSC is in the process of developing sector-specific corporate governance guidelines which will complement the Code. These guidelines will be issued for consultation in due course.

Yours faithfully

A handwritten signature in black ink, appearing to read 'M. I. Rajahbalee', is written over a horizontal line. The signature is fluid and cursive.

M. I Rajahbalee
Chief Executive