BANK OF MAURITIUS

Guideline on Corporate Governance

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INTRODUCTION

The Organisation for Economic Cooperation and Development describes corporate governance as a set of relationships between a company's management, its board, its shareholders, and other stakeholders. It provides a framework for establishing a company's objectives, means to achieve the objectives, and a monitoring process to gauge the progress being made.

Effective corporate governance is critical to proper functioning of a financial institution and, collectively, of the banking sector. Governance weaknesses can result in the transmission of problems across the entire financial sector, ultimately the economy as a whole.

The Bank of Mauritius, in its role as the supervisor of financial institutions, has a vital interest in governance practices of financial institutions under its purview. Good governance permits placing reliance on an institution's internal processes and controls. This includes effective board oversight, strong risk management, effective internal controls, compliance with statutory requirements, and related areas. In governance, the role and capacity of directors and their relationship with management play a vital role in ensuring safety and soundness of the financial institution and, in turn, safeguarding the interests of shareholders, customers and other stakeholders.

Authority

This guideline is issued under the authority of section 50 of the Bank of Mauritius Act 2004 and section 100 of the Banking Act 2004.

Scope of application

This guideline applies to banks, non-bank deposit-taking institutions and cash dealers, collectively referred to as financial institutions. Provisions marked with an asterisk (*) do not apply to cash dealers.

For the purpose of this guideline, a joint venture with a 50:50 participation in equity will not be considered as a subsidiary of a foreign bank.

Effective date

This guideline shall come into effect on 1 June 2016.

Interpretation

1. In this guideline,

(a) ‘affiliate’ has the same meaning as in the Banking Act 2004;

(b) ‘associate’ has the same meaning as in International Accounting Standard 28;

(c) ‘board’ means the board of directors of a financial institution; except that for branches of foreign banks ‘board’ means local advisory board/committee;

(d) ‘Chief Executive Officer’ means the person responsible under the immediate authority of the board of directors for the conduct of business of the financial institution;

(e) ‘executive director’ means a member of the board who is in full time employment of the financial institution;

(f) ‘non-executive director’ means a member of the board who is not an executive director and who is not associated with the day to day activities of the financial institution;

(g) ‘related party’ has the same meaning as in the Banking Act 2004; and

(h) Segment B activity is essentially directed to the provision of international financial services that give rise to “foreign source income”. Segment A activity relates to all banking business other than Segment B activity.

Structure of the guideline

There are seven sections in this guideline:

Section I - The board of directors

Section II - Responsibilities of the board of directors

Section III - Senior management

Section IV - Compliance

Section V - Internal audit

Section VI - External auditors

Section VII - Transparency

SECTION I – THE BOARD OF DIRECTORS

2. In order for the board of directors to effectively oversee the affairs of a financial institution, it must possess the necessary balance of expertise, skills, adequate knowledge of its business, and the structure and strengths of the industry it is engaged in, as well as the legal requirements impinging on the industry. The board members shall collectively possess appropriate qualifications and background for proper governance of the financial institution.

3. The board has the ultimate responsibility for the safety and soundness of the financial institution. It must oversee the institution's business strategy, internal organisation and governance structure, its risk management and compliance practices, and key personnel decisions. It is essential that there be a clear demarcation of responsibilities and obligations between the board and management. The board should be independent from management.

4. The role of the Chair of the board shall be separated from that of the Chief Executive Officer (CEO) as this is critical to maintaining the board's independence as well as its ability to execute its mandate effectively.

5. The board shall periodically conduct a self-assessment of its effectiveness as well as that of its sub-committees. This may occasionally require assistance of independent advisors.

Composition

6. Section 18(3) of the Banking Act 2004 provides that the board of directors of a financial institution incorporated in Mauritius consist of at least 5 natural persons, 40 per cent of which must be independent directors. The term 'independent' director is explained in Appendix 1. Section 18(4)(b) requires a subsidiary of a foreign bank to have 40 per cent non-executive directors instead of 40 per cent independent directors. Notwithstanding this provision, subsidiaries of foreign banks conducting largely Segment A activities shall have at least one independent director on the board and those conducting largely Segment B activities are also encouraged to have an independent director on the board.

7. Subject to the prior approval of the Bank of Mauritius, a branch of a foreign bank is strongly encouraged to establish a local advisory board/committee to carry out the functions of a board as set out in the guideline. Such advisory board/committee will ideally consist of at least 3 members, with at least one independent member.

8. A director of a financial institution may serve for a maximum term of six years. This limitation shall not apply to:

   (a) an executive director;

   (b) a non-executive director of a subsidiary of a foreign bank; and

(c) a non-executive member of the local advisory board of a branch of a foreign bank.

9. Notwithstanding the term of office of six years, an outgoing director may, with the prior approval of the Bank of Mauritius, be reappointed as director on the board of the financial institution after having observed a cooling period of two years. However, the Bank of Mauritius may, where it deems it fit, approve the reappointment of a director who has not observed the cooling period.

10. The Chairperson of the board of a financial institution shall be an independent or a non-executive director.

11. When the Chairperson is not an independent director, the board of the financial institution shall be composed of at least 50 per cent independent directors. Branches and subsidiaries of foreign banks are exempted from this requirement.

12. The CEO of a financial institution shall be a member of the board but not its Chairperson.

SECTION II - RESPONSIBILITIES OF THE BOARD OF DIRECTORS

13. The board has ultimate responsibility for the affairs of the financial institution. The board shall

    (a) approve the institution’s corporate plan covering short term and long term business objectives, strategy together with appropriate policies to execute the strategy, including those relating to risk management, capital adequacy, liquidity, risk appetite, compliance, internal controls, communication policy, director selection, and orientation and evaluation;

    (b) require management to review periodically the effectiveness of the established corporate plan and report results to the board;

    (c) appoint and monitor senior management, question and scrutinise its performance in the achievement of corporate objectives;

    (d) question, scrutinise and monitor the performance of board sub-committees, and individual directors;

    (e) ensure that policies and systems in place are effective to achieve a prudential balance between risks and returns to shareholders;

    (f) ensure that the institution has implemented effective systems and practices to achieve compliance with legal requirements, including regulations and guidelines issued by the Bank of Mauritius; and

    (g) require management to review and assess periodically the efficiency and effectiveness of policies, systems and controls and report results to the board.

14. The board shall also

    (a) be responsible for the appointment of the CEO and other senior officers, and assessing periodically their performance in the context of established corporate objectives and plans;

    (b) approve the organisation structure of the institution, and its staff compensation policies;

    (c) approve the capital and operating budgets of the institution, capital adequacy assessment process, capital and liquidity plans; and

    (d) ensure that there is a clear demarcation of duties and responsibilities between the board and management in order to implement an effective accountability regime. The board should be independent of management, holding periodically board meetings where

management officials are not present. The board shall periodically assess the CEO's effectiveness in achieving approved corporate objectives and risk appetite framework.

15. In compliance with section 48 of the Banking Act 2004 dealing with the disclosure of interest, the board shall implement policies and procedures to identify conflict of interest situations and steps to redress such situations. This shall include

    (a) an outline of potential conflict of interest situations involving different levels of staff and board members;

    (b) establishment of a process for identifying and reporting a conflict of interest situation which shall be investigated by designated officials followed by a report to management or the board, as appropriate; and

    (c) establishment of a process for ultimate decision-taking by management or the board.

16. There shall be a clear demarcation of responsibilities of the board and management. The board will set out the criteria for measuring the CEO's performance in achieving the approved corporate objectives. Such performance review shall be conducted annually. The CEO is responsible for implementing a performance and accountability regime for senior management personnel.

17. The board of directors (or by delegation, its Nomination and Remuneration Committee) shall implement a remuneration and incentive system to stimulate staff motivation to achieve the corporate objectives. The approach shall be reviewed periodically to assess its effectiveness and decide on any modifications, as necessary[1].

18. The board's primary responsibility is to protect the interests of the financial institution which it serves, and it should ensure that the decisions of the holding company/Head Office are not detrimental to the sound and prudent management of the financial institution, its financial health and the legal interests of its stakeholders.

19. The board should ensure that members participate in induction programmes and have access to ongoing training on relevant issues which may involve internal or external resources.

20. The board of directors shall meet at least once every quarter.

Board sub-committees

21. Section 18(6) of the Banking Act requires directors to establish such committees as the board deems necessary to discharge its responsibilities effectively. This will include audit committee, conduct review committee, risk management committee, and nomination and remuneration committee. Their mandates will be clearly set out and available publicly. Proceedings of sub-committees shall be reported periodically to the board.

[1] Refer to paragraph 44 for further information.

22. Notwithstanding the above, subsidiaries and branches of foreign banks may, with the approval of the Bank of Mauritius, be exempted from establishing one or more of the above mentioned committees (except, in the case of subsidiaries of foreign banks, the audit committee) after establishing that suitably effective infrastructure is in place at the parent/head office level and the Bank of Mauritius will have access to their reports as necessary.

23. The mandate and membership of each sub-committee shall be published in the financial institution's annual report.

Audit Committee*

24. Section 40 of the Banking Act 2004 requires every bank and non-bank deposit taking institution incorporated in Mauritius to establish an Audit Committee which shall comprise only independent directors who shall not be less than 3 in number.

25. The Chairperson of the board must not be the Chairperson of the Audit Committee.

26. The Audit Committee of a subsidiary of a foreign bank conducting largely Segment A activities shall have at least one independent director. Subsidiaries conducting Segment B activities are encouraged to have at least one independent director on the Committee.

27. Members of the Audit Committee should preferably have financial background and be conversant with both international auditing standards and international financial reporting standards.

28. The Audit Committee should approve the audit plans (external and internal) to ensure that these are risk-based and address all activities over a measurable cycle, and that the work of external and internal auditors is coordinated.

29. The Audit Committee, not senior management, should recommend to shareholders the appointment, removal, and remuneration of external auditors. It should also approve the engagement letter setting out the scope and terms of external audit.

30. The Audit Committee shall approve the remuneration of the Head of Internal Audit.

31. The Audit Committee should assess periodically the skills, resources, and independence of the external audit firm and its practices for quality control.

32. The Audit Committee should assess whether the accounting practices of the auditee are appropriate and within the bounds of acceptable practice.

33. The Committee should ensure that there is appropriate structure in place for identifying, monitoring, and managing compliance risk as well as a reporting system to advise the Committee and the board of instances of non-compliance on a timely basis.

34. The Audit Committee should discuss with senior management and external auditors the overall results of the audit, the quality of financial statements and any concerns raised by external auditors. This should include:

    (a) key areas of risk for misinformation in the financial statements, including critical accounting policies, accounting estimates and financial statement disclosures;

    (b) changes in audit scope;

    (c) whether the external auditor considers the estimates used as aggressive or conservative within an acceptable range;

    (d) significant or unusual transactions; and

    (e) internal control deficiencies identified during the course of the audit.

35. Further responsibilities of the Audit Committee include:

    (a) review of the audited financial statements for adequacy before their approval by the board;

    (b) assessment of whether the institution has implemented adequate internal control and financial disclosure procedures;

    (c) review of any transactions brought to its attention by auditors or any officers of the institution, or that might otherwise come to its attention, which might adversely affect the financial condition of the institution;

    (d) report to the board on the conduct of its responsibilities in frequency specified by the board, with particular reference to section 39 of the Banking Act 2004; and

    (e) ensure that management is taking appropriate corrective action in response to deficiencies identified by the auditors, including internal control weaknesses and instances of non-compliance with laws.

36. The Audit Committee must meet at least once every quarter to execute its mandate effectively.

Conduct Review Committee*

37. The duties and responsibilities of the Conduct Review Committee are set out in the *Guideline on Related Party Transactions*[2].

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[2] The guideline is available on the website of the Bank of Mauritius at https://www.bom.mu

Risk Management Committee*

38. The board shall establish a Risk Management Committee with responsibility for advising the board on the financial institution's overall current and future risk appetite, overseeing senior management's implementation of the risk appetite framework and reporting on the state of risk culture in the financial institution.

39. Risk management is critical to corporate governance. Risk may arise from direct exposures of a financial institution or through exposures of its subsidiaries, affiliates or counterparties. A financial institution should be in a position to identify risks, assess their potential impact, and have policies and controls in place to manage risks effectively. There are risks relating to liquidity, credit, operations, markets, and several other aspects of operations.

40. A financial institution must have a board-approved risk appetite framework, which is well understood throughout the organisation. All corporate, operational, and financial policies should support the framework, which should be forward-looking and consistent with the financial institution's short-term and long-term strategic plan. The framework should set benchmarks as to the acceptable risk limits, taking into account relevant financial, operational, and macroeconomic factors.

41. With the exception of the CEO, the committee members should be non-executive persons and a reasonable number should have an adequate familiarity with risk management of the financial institution. The committee should have a clear mandate from the board. The Chairperson of the board may be a member of the committee but not its Chairperson. The Chairperson of the committee shall ideally be an independent director, or, in the case of a subsidiary of a foreign bank, a non-executive director.

42. The major tasks of the Risk Management Committee include:

    (a) identification of principal risks, including those relating to credit, market, liquidity, operational, compliance, and reputation of the institution, and actions to mitigate the risks;

    (b) appointment of a chief risk officer who, among other things, shall provide assurance that the oversight of risk management is independent from operational management and is adequately resourced with proper visibility and status in the organisation;

    (c) ensuring independence of the chief risk officer from operational management without any requirement to generate revenues;

    (d) requirement of the chief risk officer to provide regular reports to the committee, senior management and the board on his activities and findings relating to the institution's risk appetite framework;

(e) receive from senior officers periodic reports on risk exposures and activities to manage risks; and

(f) formulate and make recommendations to the board on risk management issues.

43. The committee must meet at least once every quarter.

Nomination and Remuneration Committee*

44. Except for those institutions that have been granted a dispensation from this section of the guideline, each institution shall appoint a Nomination and Remuneration Committee, consisting of a majority of non-executive directors, with the following mandate:

    (a) recommend to the board candidates for board positions, including the chair of the board and chairs of the board committees;

    (b) recommend criteria for the selection of board members and criteria for the evaluation of their performance;

    (c) prepare for approval of the board the remuneration and compensation package for directors, senior managers, and other key personnel, taking into account the soundness of risk taking and risk outcomes as well as any relevant information available on industry norms;

    (d) recommend to the board an incentive package, as necessary, to enhance staff performance, while ensuring that incentives embedded within remuneration structures do not incentivise staff to take excessive risk;

    (e) recommend nominees for board committees; and

    (f) comment on the contribution of individual directors to the achievement of corporate objectives as well as on the regularity of their attendance at the board and committee meetings.

45. When considering an appointment to the board, the Nomination and Remuneration Committee shall satisfy itself that the candidate is able to commit sufficient time and effort to fulfil its responsibilities effectively, particularly if the candidate has a seat on multiple boards or undertakes other professional or commercial activities.

46. Financial institutions are encouraged to consider the use of contractual provisions to allow them to reclaim incentive components of remuneration from executive directors and key management personnel in exceptional circumstances of misstatement of financial results or of misconduct resulting in financial loss to the financial institution.

SECTION III - SENIOR MANAGEMENT

47. Consistent with the direction given by the board, senior management should implement business strategies, risk management systems, risk culture, processes and controls for managing the risks to which the financial institution is exposed and concerning which it is responsible for complying with laws, regulations and internal policies. This includes comprehensive and independent risk management, compliance and audit functions as well as an effective overall system of internal controls. Senior management should recognise and respect the independent duties of the risk management, compliance and internal audit functions and should not interfere in their exercise of such duties.

48. Members of senior management should provide adequate oversight of those they manage, and ensure that the financial institution's activities are consistent with the business strategy, risk appetite and the policies approved by the board.

49. Senior management is responsible for delegating duties to staff. It should establish a management structure that promotes accountability and transparency throughout the financial institution.

50. Senior management should provide the board with the information it needs to carry out its responsibilities, supervise senior management and assess the quality of senior management's performance. In this regard, senior management should keep the board regularly and adequately informed of material matters, including: changes in business strategy, risk strategy/risk appetite; the financial institution's performance and financial condition; breaches of risk limits or compliance rules; internal control failures; legal or regulatory concerns; and issues raised as a result of the financial institution's whistleblowing procedures.

51. The CEO shall be directly responsible for the day to day operations of the financial institution and shall be conversant with the state of internal control, the prevailing legislation as well as current issues impinging the financial sector.

SECTION IV - COMPLIANCE

52. A financial institution must function with integrity and in compliance with laws, regulations, and policy directives of management. While the board has the ultimate responsibility for ensuring compliance, management must establish the parameters of compliance policy and its modus operandi. This would include identification of compliance risks and how these have to be managed throughout the organisation. To be effective, the compliance function must have adequate authority, resources, independence and stature in the organisation.

53. A financial institution must establish an administrative framework to advise management and the board on an ongoing basis on the financial institution's compliance with applicable laws, regulations and the board directives. The framework may involve establishing decision points for resolving non-compliance issues as they arise.

54. It is to be recognised that compliance function is independent from management to avoid any undue influence or obstruction in the conduct of its responsibilities. The compliance function should report directly to the board of directors or a committee of the board and have an easy access.

SECTION V - INTERNAL AUDIT

55. Internal audit provides independent assurance to the board and senior management on whether

    (a) the internal control system in place is performing effectively and is adequate to mitigate risks consistent with the risk appetite of the financial institution; and

    (b) the organisational goals are met and corporate governance processes are effective and efficient.

56. Every financial institution shall set out the mandate of internal audit, defining its purpose, authority and responsibilities. The board and management must contribute to the effectiveness of the internal audit function by:

    (a) setting out clearly its role and responsibility for governance, compliance, risk management and fraud investigation;

    (b) requiring internal auditors to develop an annual work plan to provide adequate coverage of critical operations over an agreed upon timeframe;

    (c) requiring internal auditors to report directly to the Sharia Advisor/Sharia Supervisory Board to ensure independence from management;

    (d) providing internal audit full access to any records, files, management information systems, minutes of various committees, including the audit committee, as well as physical properties of the financial institution;

    (e) providing internal audit authority, among other things, to independently assess the effectiveness of internal control, risk management and governance systems;

    (f) requiring internal auditors to adhere to international professional standards, such as those of the Institute of Internal Auditors;

    (g) ensuring that the internal audit staff has adequate professional background and training to carry out responsibilities effectively;

    (h) ensuring that the internal audit reports are transmitted to the board and audit committee without any undue filtering of findings by management, and that the reports include a timeframe within which corrective action must be taken; and

    (i) requiring the board and management to provide timely and effective response to the findings of internal auditors.

57. The head of the internal audit department shall not be responsible for any other function in the financial institution.

58. Compliance risk should be included in the risk assessment methodology of the internal audit function, and an audit programme that covers the adequacy and effectiveness of the financial institution's compliance function should be established. This principle implies that the compliance function and the audit function should be separate, to ensure that the activities of the compliance function are subject to independent review.

SECTION VI - EXTERNAL AUDITORS

59. Section 39 of the Banking Act 2004 deals with the appointment, powers and duties of external auditors of financial institutions.

60. The board of a financial institution shall ensure that external auditors

    (a) maintain a high standard of auditing and professional conduct;

    (b) have complete independence, in fact and in appearance, from management and their audit programs are in no way influenced by management;

    (c) have no pecuniary relationship, individually or collectively, with the financial institution or a related party that might compromise their independence; and

    (d) bring to the attention of management as well as the supervisor any matters that require urgent action. This will include, among other things, material adverse changes in the risks of a financial institution's business, breach of laws and regulations, serious conflicts between decision makers within the financial institution.

61. A financial institution may engage the firm responsible for its audit to provide non-audit services. This may be done with the prior approval of the audit committee which will ensure that the non-audit work does not entail any conflict with the audit work. Furthermore, the firm's partner responsible for non-audit work should have no responsibility for the audit of the financial institution and the remuneration for the non-audit work must be based on the complexity and duration of work.

62. The financial institution's annual report shall disclose separately the audit and non-audit fees paid to the audit firm. It shall also disclose any fees paid to the audit firm by a subsidiary or associate of the financial institution.

63. The engagement partner, the audit review partner, the audit manager or a person with similar responsibilities in the audit firm who were directly involved in the audit of a financial institution shall not be appointed to a senior level position in the financial institution until or a period of three years has elapsed from the end of their last audit assignment.

SECTION VII - TRANSPARENCY

64. Governance practices must be adequately transparent to shareholders, depositors and other market participants. They need complete and timely information on significant activities to hold a financial institution's board and senior management accountable for the trust placed in them to achieve corporate objectives.

65. The level of disclosure will vary depending on the size, structure, complexity of operations, economic significance and risk profile of a financial institution. However, as a minimum, a financial institution must disclose the board selection process as to the skills, background and experience essential to guide the financial institution's affairs and to protect interests of shareholders. It should also disclose the financial institution's management infrastructure, including the board committees and their mandates and the number of times they have met.

66. Other information for disclosure includes a description of a financial institution's objectives, governance structure and policies, major shareholdings and voting rights, related party transactions, remuneration and compensation policy, including criteria for performance measurement. The board should disclose the remuneration/fees of directors, senior executives and key employees. Disclosure should be timely, accurate, clear and easily understandable to inform all stakeholders effectively.

67. As previously mentioned, a financial institution should disclose on an annual basis key aspects of risk exposure and risk management and controls. In addition, a financial institution must disclose any direct and/or indirect shareholdings of a person aggregating ten percent or more.

APPENDIX 1

"Independent director" as defined in the Banking Act 2004 means a director having no relationship with, or interest in, whether past or present, the financial institution or its affiliates, which could or could reasonably be perceived to materially affect the exercise of his judgment in the best interest of the financial institution.

For avoidance of doubt, the following, shall

(i) be considered as an independent director

1. A director who has not been employed by the financial institution or the group of which it currently forms part of, in any executive capacity for the preceding 3 financial years.

2. A director who has not been employed by any other financial institution regulated by the Bank of Mauritius in an executive capacity for the preceding 3 financial years.

3. A director who is not a related party to an individual who is or has been in any of the past 3 financial years employed by the financial institution or the group in an executive capacity.

4. A director who is not an adviser to the financial institution or the group other than as a member of the board.

5. A director who has no relationship or interest in the financial institution or group which could or could reasonably be perceived to materially affect the exercise of his judgement in the interest of the financial institution.

(ii) not be considered as an independent director

1. A director of an immediate and/or ultimate holding company shall not be considered as an independent director of the financial institution.

2. A director of a company which holds 10 per cent or more of the shares of a financial institution shall not be considered as an independent director of the financial institution.

3. A director of a company in which a financial institution holds 20 per cent or more of its shares shall not be considered as an independent director of the financial institution.

4. A former employee receiving a pension or any other benefits from a financial institution will not be considered as an independent director for that institution irrespective of the number of years since his retirement.