

# The Core Code of Corporate Governance: Requirements and Recommendations

## Foreword

The Ukraine Code of Corporate Governance was first issued in 2003. This is a substantially re-written third edition that is designed to reflect global developments in corporate governance since the prior edition and simplify the structure and recommendations with a view towards encouraging better implementation.

In late 2018, the National Securities and Stock Market Commission of Ukraine (NSSMC) agreed with the Ukrainian Corporate Governance Academy (UCGA) to draft a set of recommended corporate governance practices for listed companies in Ukraine. From the outset, it was decided that the resulting Code would be developed in close collaboration with Ukrainian listed companies and foreign and domestic investors to ensure that it would be realistic and practical, respond to investor expectations and reflect best practice.

Acknowledgments are due to the companies, investors and other stakeholders who contributed their views and time to this important project. IFC and SECO<sup>1</sup> are thanked for their generous support and the contribution of valuable expertise. Special thanks are given to Richard Frederick, an independent governance consultant, who guided the strategy and the process behind the Code and its drafting. All of the individuals who contributed to the Code did so in their personal capacities. The Code does not necessarily reflect the views of the all individual participants or the institutions with whom they might be affiliated.

**Disclaimer:** The content of this Code should not be construed as legal or financial advice. Neither the UCGA, the NSSMC, IFC, SECO or any of the individuals associated with the project make any representation whatsoever within this document regarding extant law or any other regulations or rules that might relate to the governance of Ukrainian companies. Any mention of law and regulation herein is purely for illustrative purposes. The Code does not purport to be either up-to-date or complete where laws, regulations or rules are mentioned. It is exclusively the responsibility of companies to ensure that they are informed of and in compliance with extant law. This Code was completed as of January 1, 2020.

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<sup>1</sup> SECO - Swiss State Secretariat for Economic Affairs.

## Summary

The structure of the Code and a summary of its intended outcomes are as follows:

### 1. Company objectives

The Company creates long-term sustainable value and maximises returns to its Shareholders. It does so by increasing the value of its shares and by paying dividends.

### 2. Shareholders rights and the role of other Stakeholders

**2.1. Shareholder rights:** The Shareholder rights found in law, regulation and listing requirements are fully respected. In addition, the Company ensures that the spirit of the law, which aims at the equitable and fair treatment of all Shareholders, is respected.

**2.2. General Shareholders Meetings:** Shareholders have the ability to exercise their legal rights, and participate and vote at the GSM in order to express their views and protect their interests.

**2.3. Company engagement with Shareholders:** Shareholders are able to engage and communicate with the Company to express their concerns and protect their legitimate interests.

**2.4. Takeovers:** The process of takeover is transparent and fair.

**2.5. The role of other Stakeholders:** The Company is aware of best practices with respect to Stakeholder relations and seeks to implement such practices to the extent possible. The Company complies with all relevant legislation designed to protect Stakeholders and encourage Stakeholder engagement.

**2.6. Sustainable Development:** The Company is aware of best practices with respect to Sustainable Development and seeks to implement such practices to the extent possible. The Company complies with all laws designed to enhance Sustainability Development.

### 3. The Board

**3.1. Commitment:** Board Members actively contribute to the governance of the Company and to achieving the Company's objectives.

**3.2. The fiduciary duties of the Board:** The Board is responsible, effective, and accountable and acts exclusively in the interests of the Company and its Shareholders.

**3.3. The roles and responsibilities of the Board:** The Board exercises its expected roles.

**3.4. Board composition:** The Board has the competencies, experience, independence and diversity necessary to fulfil its duties, roles and responsibilities.

**3.5. Independence:** The Board is objective and fair, and acts independently of special interests and Management in the best interests of the Company and all of its Shareholders.

**3.6. Fit and proper testing:** Board Members have an impeccable reputation and the knowledge, skills and experience to effectively support to the role of the Board.

**3.7. Nominations and appointments:** The nominations and appointment process is fair, formal, open and transparent.

#### 3.8. Training:

*Induction training:* Board Members are sufficiently informed regarding their fiduciary duties, their roles, good governance practices and the nature and strategic challenges of the Company as soon as they take up their posts.

*Ongoing training:* Board Members have up-to-date knowledge and skills to help them contribute effectively to the fulfilment of their roles.

**3.9. The Board Chair:** The Board has effective leadership.

**3.10. The Corporate Secretary:** The Board has the administrative support it requires and access to expert advice on governance and compliance matters so as to be able to effectively fulfil its responsibilities.

**3.11. Board committees:** The Board has the committee support it needs to optimally fulfil its roles and responsibilities.

*The Audit Committee:* The control environment of the Company is subject to effective independent oversight such that Stakeholders have assurances that the Company has reliable controls and reporting.

*The Nominations Committee:* The Company has the best possible human resources available to staff its Board and Management and is able to ensure stable leadership through effective human resource management and succession planning.

*The Remuneration Committee:* The Company has remuneration practices that are fair and help attract and retain the human talent it needs for its Board and Management. Management and staff are incentivised to achieve the Company's objectives and the Company recognises its Management and staff for good performance. The Company is accountable to Shareholders for its remuneration practices.

**3.12. Remuneration:** The remuneration of Board Members and Management is transparent, fair and sufficient to attract, motivate and retain talent.

**3.13. Board size:** The Board has a size that supports the fulfilment of its roles and responsibilities and its composition goals.

#### 4. Co-operation between Management and the Board

The Company has effective Management that is accountable to both the Board and Shareholders for the achievement of Company objectives. The Board and Management have distinct roles and responsibilities. They collaborate effectively to the benefit of the Company and do not infringe on each other's roles or responsibilities.

#### 5. Disclosure and transparency

**5.1. Communications with Shareholders:** The Shareholders and the markets have timely and fair access to all information that is material to their investment decisions and such information is presented in a balanced fashion.

**5.2. Financial reporting:** Information on the financial performance and position of the Company is objective, reliable and clear and Shareholders are satisfied that they have sufficient information to inform their investment decisions.

**5.3. Non-financial reporting:** Relevant non-financial Information, including on the governance of the Company, is provided to Shareholders and the markets to better inform their investment decisions. The impact of the Company on society and the environment is made clear to stakeholders.

**5.4. The independent external audit:** Shareholders, stakeholders and the markets have full confidence in the quality of the Company's financial and non-financial reports.

**5.5. Dividends and Dividend Policy:** The dividend policy is clear to Shareholders and the markets.

**5.6. The Company website:** All information destined to Shareholders, the markets and other Stakeholders is well-organised and made easily available on the Company website.

## 6. The control environment and ethical standards

**6.1. Internal controls:** The system for internal control provides assurances that the Company has adequate controls over operations, financial reporting and compliance matters.

**6.2. Risk management:** Risk management provides companies and investors a high degree of confidence in their decisions. The process of risk management detects, analyses and controls risks and mitigates possible circumstances that could have a negative impact on achieving company objectives.

**6.3. Compliance:** The Company complies with internal rules, policies and procedures and external law and regulations.

**6.4. The internal audit function:** The internal audit function provides independent assurances that the Company has in place an effective internal control system, risk management and a compliance function.

**6.5. The Ethics Code:** The Company, its Board, Management and staff act ethically and with integrity.

**6.6. Anti-corruption Policy:** The Company does not engage in any corrupt practices and is seen as being honest and law-abiding.

**6.7. Conflict of Interest Policy and Related-party Transaction Policy:** The Company and its Shareholders are protected from abuses arising from conflicts of interest.

## 7. Corporate governance evaluations

The Company is abreast of trends in good governance and ensures a continuing cycle of improvement in its governance practices.

## Introduction

### The definition of corporate governance

Corporate governance is the system of rules, practices, and processes by which the objectives of the Company are set, the means of attaining those objectives are decided, and the monitoring of performance occurs. Good governance demands accountability for the achievement of the ultimate goal of the Company which is to generate long-term shareholder value. Good governance is defined by a large number of practices and structures which, jointly, contribute to the achievement of the Company's goals.

### The case for good governance

Good governance helps to increase the Company's value by enhancing its competitiveness, efficiency and growth. Good governance strengthens confidence in the Company and helps encourage value creation in the interests of shareholders, employees and other stakeholders.

### The purpose of the Code

This Code is intended to strengthen the confidence of investors in Ukraine's listed companies and strengthen confidence in Ukraine's capital market. It spells out the basic requirements set down under law and regulation, and adds best practice recommendations that are designed to meet the expectations of investors. It also defines the distinct roles of shareholders, boards and management in the governance and operations of the Company. And, finally, it discusses the role of other stakeholders in the Company and the Company's commitment to achieving sustainable development.

### The target audience

The Code applies first and foremost to the companies listed on Ukraine's stock markets that fall under the supervision of the NSSMC.<sup>2</sup>

The Code also provides guidance to unlisted companies which constitute a significant part of Ukraine's economy. The Code is particularly relevant to companies that are contemplating a future listing. Companies that adapt their governance practices to the Code prior to listing are expected to have more successful public offerings. The Code is also relevant to state-owned enterprises (SOEs) for whom private sector corporate governance practices remain an important reference point.

In the event that a recommendation of this Code conflicts with law or a more specialised set of recommendations (such as the UCGA Recommendations on the Governance of SOEs), then the law and/or the specialised recommendations should prevail.

The Code is designed to address the governance practices of both unitary and two-tier boards. A two-tier structure refers to a Board composed exclusively of non-executives that oversees a "management board" composed exclusively of executives. The Code applies equally to unitary boards that combine both executives and non-executives into one body. Both the Supervisory and the unitary boards are referred to simply as a "Board" throughout the Code. Whatever the board structure, the body of

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<sup>2</sup> Shareholders will also find this Code of interest though the Code includes no requirements or recommendations on how shareholders should exercise their role in the governance of the enterprise. The NSSMC and UCGA intend to issue guidance on the roles and responsibilities of shareholders in corporate governance in future.

managers, whether a formally constituted “management board” or not, is referred to simply as “Management” in the Code.

The Board is responsible for the governance of the Company and should evaluate how to respond to the recommendations of the Code. Along with the Board, Management will play an important role in implementing the Code’s recommendations.

### International standards

This Code adheres to the *G20/OECD Principles of Corporate Governance*<sup>3</sup> which are the international reference point for good corporate governance. In addition, the Code reflects the recommendations of the *Final Report on Corporate Governance*<sup>4</sup> of IOSCO’s Growth and Emerging Market Committee. The IOSCO report provides essential insights into the priorities and practices of securities exchange regulators worldwide with respect to the governance of listed companies. Recommendations on disclosure follow those of the United Nations Conference on Trade and Development (UNCTAD) *Guidance on Good Practices in Corporate Governance Disclosure*.<sup>5</sup> The *IFC Corporate Governance Methodology*<sup>6</sup> and various national codes were also consulted and served as inspiration for the Code.

### The structure of the Code

The Code identifies governance practices that are considered essential for good governance. For each practice, the following are provided:

- *The Goal*: The intended outcome of the practice
- *Requirements*: Legal, regulatory and listing requirements
- *Recommendations*: Recommended best practices
- *Comments*: Additional details and alternatives

### Relationship between the Code, law, regulation and listing requirements

The Requirements section summarises the legal, regulatory and listing requirements that companies *must* follow. Such requirements are always obligatory. Because law, regulations and listing requirements change, it is not possible to ensure that the Requirements referenced in the Code are complete or up-to-date. Companies must, therefore, assure themselves that they are in full compliance with extant rules.

The Recommendations section proposes practices that go beyond the minimum required by law, regulations and listing rules. It suggests good practice where the law is silent. Companies *should* follow the Recommendations but can choose when and how to implement them. There is an expectation that companies will comply with the Recommendations of the Code.

### Enforcement

The method by which this Code is enforced is through disclosure. The law requires Ukrainian joint-stock companies and listed companies to make annual corporate governance disclosures. The USSMC has

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<sup>3</sup> See OECD website at: <http://www.oecd.org/corporate/principles-corporate-governance/>

<sup>4</sup> See IOSCO reference to FR10/16 Report on Corporate Governance, Report of the Growth and Emerging Markets Committee of IOSCO 3/10/2016 at: [https://www.iosco.org/publications/?subsection=public\\_reports](https://www.iosco.org/publications/?subsection=public_reports)

<sup>5</sup> See UNCTAD website at: <https://unctad.org/en/pages/publicationarchive.aspx?publicationid=261>

<sup>6</sup> See IFC website at: [https://www.ifc.org/wps/wcm/connect/topics\\_ext\\_content/ifc\\_external\\_corporate\\_site/ifc+cg/investment+services/corporate+governance+methodology](https://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/ifc+cg/investment+services/corporate+governance+methodology)

established this Code as the relevant reference point for reporting. Companies are required to explain how they implement the Recommendations of the Code in the Company's annual report or in an *Annual Report on Corporate Governance* wherein they must identify any departure from the Code. If a Company does not comply with the Recommendations, it must explain its reasoning for not complying and describe any alternative practices used to achieve the governance Goal. Even when companies comply fully with the Code's Requirements and Recommendations, they must provide a self-evaluation and a discussion for each of the chapter headings in the Code. The disclosure must be published in a clearly identified section of the Company's website dedicated to corporate governance.

### Flexibility and proportionality

While the Code is intended mainly for listed companies, there is also the expectation from the NSSMC that unlisted companies will implement its Recommendations. For all companies (but for unlisted companies in particular), the Recommendations of the Code are intended to be implemented flexibly and proportionally. This means that companies ultimately decide how they achieve the Goals set out in this Code. The intent of flexible and proportional implementation is to avoid over-regulation, unenforceable laws, or other unintended consequences that may unduly burden businesses.

Flexible and proportional implementation does not mean that the governance practices of a company are any worse. On the contrary, the principles of flexibility and proportionality can make implementation more appropriate and enforcement more effective by tailoring the Code's recommendations to the circumstances of the company. In addition, it is hoped that by permitting the flexible and proportional implementation of the Code that a wider set of companies will embrace better governance.

### How to disclose

Companies are encouraged not to take a legalistic approach to their *Annual Report on Corporate Governance* or their reporting to the NSSMC. They should take the time to describe their practices and use disclosure as an opportunity to demonstrate the quality of their governance rather than simply stating that they comply. In addition to disclosing an *Annual Report on Corporate Governance*, all listed companies are enjoined to make a public declaration of their commitment to the Code. The NSSMC have provided simplified disclosure forms for unlisted companies to guide them in their disclosure.

### Supplements to the Code

This Code was written to be concise and focus on essential "core" issues in governance. However, many issues covered in this core Code stand to benefit from further discussion and guidance. For this reason, the NSSMC and the UCGA plan to provide supplements to the Code and provide additional recommendations on related topics including:

- The role of shareholders and institutional investors in corporate governance
- Governance and sustainable development
- Audit committees
- Nominations practices for Board Members
- The governance of unlisted companies
- The governance of remuneration
- Risk governance and risk management
- Compliance
- Conflicts of interest and related-party transactions
- Anti-corruption practices
- The whistle-blower function
- Model policies and documents



The plan is for the NSSMC and the UCGA to supplement this core Code with regular releases of recommendations over time.

## Requirements and Recommendations

### 1. Company objectives

*The Goal:* The Company creates long-term sustainable value and maximises returns to its Shareholders. It does so by increasing the value of its shares and by paying dividends.<sup>7</sup>

*Requirements:* Company law requires that Board Members act for the benefit of the Company and its Shareholders. This requirement is embodied in the duties of care and loyalty that Board Members have to the Company (See the fiduciary duties of the Board 3.2). The Requirement may also be reflected in the Company Charter and By-laws.

*Recommendations:*

- *Documentation:* The Company Charter and/or By-laws should mention the goal of generating long-term sustainable value for the benefit of the Company and its Shareholders.

*Comments:* All companies have the objective of maximising shareholder value or long-term sustainable value. This high-level goal is supported by strategies and business plans that vary from company to company. The way that this goal is achieved also varies between industries and company types. Listed firms tend to be singularly focused on this objective. But, other companies, such as banks, do so within a tight regulatory framework that seeks to guarantee the stability of the financial system and protect the interests of stakeholders such as depositors. Further, state-owned enterprises (SOE) usually aim at public policy objectives in addition to shareholder value objectives. SOEs still aim at maximising long-term sustainable value albeit for a broader group of stakeholders and not just shareholders. Though there is more and more public pressure for companies to be run in the wider interests of stakeholders, a clear commitment to shareholder value is of overriding importance to investors.

### 2. Shareholders rights and the role of other Stakeholders

#### 2.1. Shareholder rights

*The Goal:* The Shareholder rights found in law, regulation and listing requirements are fully respected. In addition, the Company ensures that the spirit of the law, which aims at the equitable and fair treatment of all Shareholders, is respected.

*Requirements:* The law gives Shareholders rights including to: transfer shares; participate in the profits of the Company (including through dividends); participate and vote at the General Shareholders Meeting (GSM); vote on fundamental decisions (such as the termination or alteration of the Company's activities, significant amendments to the Company Charter, authorising additional shares); elect and remove Board Members; receive material information on the Company; pre-emptive rights; and the right to appeal GSM decisions in court. The law also requires that all Shareholders of the same class of shares should be treated equally and that the principle of "one-share, one vote" must apply.

*Recommendations:*

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<sup>7</sup> Sustainability objectives and the Company's relationship with its broader group of Stakeholders are discussed in Section 2.5.

- *Board:* The Board should ensure fair treatment of Shareholders and should not permit any abuse of their rights
- *Foreign Shareholders:* Foreign investors should have the same opportunity to participate in the governance of the Company as domestic investors.
- *Minority Shareholders:* Minority Shareholders should have the same opportunity to participate in the governance of the Company as larger Shareholders.
- *Accountability:* Shareholders should be able to hold the Board and Management to account for Company performance through disclosure (See Disclosure and transparency 5.0) and participation at the GSM (See General Shareholders Meetings 2.2).
- *Facilitation of rights:* The Company should facilitate Shareholders in the exercise of their rights and, in particular, their participation at the GSM.
- *Disclosure:* The Company should provide Shareholders with the information necessary to hold the Board and the Company accountable.

*Comments:* One share, one vote is a governance principle that gives all shareholders equal rights and where the only differences between shareholders results from the number of shares they hold. Notwithstanding the one-share, one-vote principle, Ukraine permits cumulative voting whereby shareholders can allocate all their votes to one board candidate or divide them among several. Cumulative voting helps minority shareholders concentrate their votes to improve their chances of representation on a board. Given that the main purpose of the Code is to strengthen investor confidence in Ukraine’s capital market and to provide confidence to foreign investors, it is essential that foreigners suffer no disadvantages compared to domestic investors. Though some of the above recommendations exist in law, companies and their boards can do much to ensure that shareholder rights are not just superficially acknowledged but, rather, that their spirit is respected and that rights are easily asserted.

## 2.2. General Shareholders Meetings

*The Goal:* Shareholders have the ability to exercise their legal rights, and participate and vote at the GSM in order to express their views and protect their interests.

*Requirements:* The law permits Shareholders or their representatives to participate in person in the GSM. Specific Shareholder rights and requirements include: meeting notice of a minimum of 30 days; requirement to hold the GSM in Ukraine (except where the Company is wholly foreign-owned); the right to submit written questions before the GSM and receive written responses; disclosure of voting results at the GSM and formal confirmation of results within 10 days.

*Recommendations:*

- *Information:* Persons who have the right to attend the GSM should be: a) notified of the agenda, rules and procedures, resolutions; and b) provided with sufficient supporting information to allow them to form an educated view on all matters to be considered at the GSM a minimum of 30 days before the GSM.
- *Venue:* Companies should hold their GSM at the Company’s registered seat or in a location easily accessible to Shareholders.
- *Board candidates:* The identity and background of candidates should be disclosed simultaneously with the notice of the GSM.

- *Electronic voting:* Voting in absentia was restricted in Ukraine. In future, the Company should facilitate electronic voting, including the electronic distribution of proxy materials.
- *Attendance:* The CEO, the CFO, the majority of the Board, and the external auditor should attend at least annual GSM.
- *Questions:* Shareholders should have the right to ask oral questions with regard to the agenda at the GSM and receive answers.
- *Documentation:* The rules and procedures that govern the conduct of the GSM should be set down in the Company Charter and/or By-laws.
- *Disclosure:* GSM proceedings and decisions (including the number of votes cast for and against each resolution) as well as the answers to significant questions of relevance to shareholders that are posed at the GSM should be disclosed within 5 working days of the GSM.
- *Website:* The Company should use its website to provide all the information necessary to Shareholders to facilitate their participation in the GSM and inform them of its conclusions.

*Comments:* One of the roles of a board is to ensure that shareholders have the opportunity to participate effectively in the GSM. Given the importance of attracting foreign investors to Ukraine's securities markets, it is important to minimise any impediments to the voting of foreign investors. Under the *G20/OECD Principles*, any prohibitions on voting in absentia, the requirement of personal attendance at GSMs to vote, holding the GSM in a remote location, or allowing voting by show of hands would not be considered good practice. Ukrainian law permits voting by proxy. Practices such as postal voting and internet voting may be considered the most conducive to encouraging shareholder participation in the governance of the company.

### 2.3. Company engagement with Shareholders

*The Goal:* Shareholders are able to engage and communicate with the Company to express their concerns and protect their legitimate interests.

*Requirements:* There are no legal requirements regarding the establishment of an Investor Relations Contact Point or the development of a Shareholder Engagement Policy that serve to facilitate the interaction between the Company and its Shareholders.

*Recommendations:*

- *Policies:* The Company should have a Shareholder Engagement Policy that lays down the parameters of the Company's interaction with Shareholders. The policy should be approved by the Board.
- *Contact point:* The Company should establish a formal mechanism (an investor relations function or contact point) that can respond to investor inquiries and facilitate Shareholder participation in the governance of the Company and participation at the GSM and ensure that minority shareholders have the ability to have their views heard by the Board.
- *Disclosure:* The Company should disclose its Shareholder Engagement Policy on its website.

*Comments:* Best practices suggests that companies facilitate shareholder participation in any decision that fundamentally impacts the company or the interests of its shareholders. It is essential that companies be transparent about their governance practices in order to achieve this goal. Not all companies can establish a full-fledged investor relations department and may find it more practical to assign that role to an existing function such as that of a Corporate Secretary (See Corporate Secretary

3.10) or a press or legal department. Shareholder Engagement Policies are increasingly posted by leading companies on their websites. The NSSMC and UCGA plan to develop a model Shareholder Engagement Policy as part of their future work on Model Policies and Documents. In order to reduce documentation requirements, it is possible to combine the Company's Shareholder Engagement Policy with its Disclosure Policy (See Communications with Shareholders 5.1).

#### 2.4. Takeovers

*The Goal:* The process of takeover is transparent and fair.

*Requirements:* There are no limitations on Boards or Management in their use of hostile takeover defences.

*Recommendations:*

- *Policies:* The Board should establish guiding principles for how it will act in the event of a takeover bid.
- *Takeover defences:* The Board should not exercise mandates or pass any resolutions with the intent of obstructing a take-over unless approved by the GSM.
- *Advice:* The Board and Management should present Shareholders with a balanced analysis of the merits of any takeover bid.
- *Approval:* Acceptance or rejection of takeover bids should be decided by the Shareholders.

*Comments:* Corporate takeovers can be either friendly or hostile. In a friendly takeover, the acquirer negotiates with the management. But, when an acquirer believes management is not maximising shareholder value, they may make an offer directly to shareholders for their stock at a premium to the market price. This is called a hostile takeover. The threat of a hostile takeover may, in turn, cause the target company's board to deploy a takeover defence. There are different opinions regarding the desirability of corporate takeovers and takeover defences. Some see it as a way to liberate locked-in shareholder value while others see it as a way for acquirers to unjustly appropriate themselves of a company with potentially damaging effects on management and employees. From a shareholder perspective, the price of a company's shares tends to rise upon a takeover bid and decline with a successful takeover defence. Over recent years, shareholder advocates and activist investors have moved to block boards from adopting take-over defences.

#### 2.5. The role of other Stakeholders

*The Goal:* The Company is aware of best practices with respect to Stakeholder relations and seeks to implement such practices to the extent possible. The Company complies with all relevant legislation designed to protect Stakeholders and encourage Stakeholder engagement.

*Requirements:* There are no legal requirements for boards to take into account or consider Stakeholder interests. However, there is ample legislation that protects Stakeholder rights (such as labour and insolvency law). Companies must comply with all relevant laws designed to protect Stakeholders.

*Recommendations:*

- *Good faith:* The Company should act in good faith (hold a sincere intent to be fair, open, and honest) towards all of its Stakeholders.

- *Standards:* The Company should keep up-to-date with best-practice standards of Stakeholder relations.
- *Policies:* The Company should have a Stakeholder Engagement Policy or a Code of Conduct that specifies how the Company will interact with its Stakeholders. The policy should be approved by the Board.
- *Stakeholder engagement:* The Board and Management should identify the Stakeholders that contribute to the Company's profitability, performance and Sustainable Development and devise strategies for how to engage with Stakeholders in pursuit of common interests. The Board should determine which stakeholders they need to engage with directly.
- *Reporting:* The Company should report regularly on its Stakeholder relations and publish regular reports on its website.

*Comments:* A stakeholder is a person, group or organisation that has an interest in the company. Stakeholders can affect or be affected by the company's actions, objectives and policies. Some examples of stakeholders are creditors, employees, government, shareholders, suppliers, unions, and the local community. At times, the interests of the company and its shareholders can conflict with the interests of other stakeholders. In such cases, a company and its board are always obliged first to obey the law and, unless there is legislation to the contrary, the law will require boards and management to act in the interest of the company. This does not prevent the board or the company from taking a nuanced view on the interaction between the company and its stakeholders since their interests often coincide over the long term. So, for example, it may be possible for the company to temporarily enhance its profitability by offering consumers less, by ignoring environmental concerns or by not investing in worker's safety. However, over the longer term, disregarding stakeholders can have a profound impact on the reputation of the company and its interactions with the stakeholders and the interest groups on whom its long-term success ultimately depends.

## 2.6. Sustainable Development

*The Goal:* The Company is aware of best practices with respect to Sustainable Development and seeks to implement such practices to the extent possible. The Company complies with all laws designed to enhance Sustainability Development.

*Requirements:* There are no legal requirements for boards to take into account or consider issues of Sustainable Development. There is, however, legislation that protects the environment. Companies must comply with environmental legislation and all other laws designed to encourage sustainable development.

*Recommendations:*

- *Commitment to Sustainable Development:* The Board and Management should consider how the Company can contribute to achieving the goals of Sustainable Development while simultaneously achieving Company objectives (See Company objectives 1.0).
- *Responsible conduct:* The Company should act responsibly towards the environment and in good faith in achieving the goals of Sustainable Development.
- *Standards:* The Company should keep up-to-date with best-practice standards in Sustainable Development.

- *Policies:* The Company should develop a Sustainable Development Policy that describes how the Company plans to interact with its environment and also considers potential risks related to the environment. The Sustainable Development Policy should be approved by the Board.
- *Reporting:* The Company should report on its policies and actions with respect to Sustainable Development and publish regular reports on its website.

*Comments:* Sustainable development aims at conducting economic activity in the present without compromising the health and welfare of future generations. The central goal of sustainable development is economic and social progress without extinguishing the globe's limited resources or destroying the natural environment. Yet, the goal of sustainable development is also broader. Sustainable development also aims at encouraging greater human welfare and a healthier and more just society. Sustainable development is sometimes viewed as an effort to balance the positive and negative outcomes of economic activity. Until the second half of the 20<sup>th</sup> century, what economists refer to as the "negative externalities" of economic activity, received comparatively less attention and less commitment from businesses and policy makers compared to economic growth. This relative inattention certainly contributed to the current environmental crisis. Today, many believe that in order to achieve sustainability, governments need to take the lead. Yet, companies have a role to play in rectifying many problems. Companies have traditionally been the main engine of economic growth and, as contributors to the environmental crisis, can also be seen as part of the solution. Precisely what the obligations of companies are in addressing the concerns of sustainable development is the object of ongoing debate. At present, many of the efforts to encourage sustainable development by companies are voluntary and lack the incentives created by law. Nevertheless, the action and commitment of companies is important as clearer and more forceful national and international rules emerge.

### 3. The Board

#### 3.1. Commitment

*The Goal:* Board Members actively contribute to the governance of the Company and to achieving the Company's objectives.

*Requirements:* There are no legal requirements regarding commitment nor with respect to the capacity of Board Members to fulfil their obligations to the Company.

*Recommendations:*

- *Leadership:* Boards should actively promote good governance practices and a good governance culture.
- *Expression of commitment:* The Board should publicly express its commitment to achieving the Goals of this Code in the Company's Annual Corporate Governance Report.
- *Availability:* Board Members should allocate sufficient time to the Company to discharge their responsibilities effectively.
- *Other board seats:* Board Members should not have more than 3 additional Board seats at other enterprises.
- *Monitoring:* The Company should take attendance records for Board and committee meetings and disclose attendance in its Annual Report or Annual Corporate Governance Report.

*Comments:* Commitment means being dedicated to a cause. In the context of this Code, it means being dedicated to the cause of improving the company's governance. Commitment cannot be achieved by simply drafting a policy. It is a state of mind, an intangible quality, that is, nevertheless, essential. Commitment is similar to leadership. Without it, plans and policies may never be implemented. Both commitment and leadership are difficult to assess and measure. However, indications of commitment to good governance can be found in all of the activities of management and the board when these are fully dedicated to achieving company goals.

### 3.2. The fiduciary duties of the Board

*The Goal:* The Board is responsible, effective, and accountable and acts exclusively in the interests of the Company and its Shareholders.

*Requirements:* Company law sets down the fiduciary duties of Board Members. It establishes the duties of loyalty and care and requires Board Members to be informed and diligent and act exclusively in the interest of the Company and its Shareholders.

*Recommendations:*

- *Documentation:* The Company Charter, the By-laws or a board charter should refer to and explain the duties of care and loyalty of Board Members.
- *Training:* All Board Members should understand their fiduciary duties and should receive induction training that covers their fiduciary duties (See Training 3.8).
- *Information:* The Board has a duty to act on an informed basis and, as a consequence, should demand any and all information that it reasonably feels it needs to effectively fulfil its duties. Management should be proactive in furnishing such information to the Board (See Co-operation between Management and the Board 4.0).
- *Conflicts of interest:* The Board should have policies and systems in place to manage conflicts of interest (See Conflict of Interest Policy and Related-party Transaction Policy 6.7).
- *Evaluation:* The Board should consider the extent to which it complies with its duties in an annual governance evaluation and develop remedial plans as needed (See Corporate governance evaluations 7.0).

*Comments:* The duties of a board are distinguished from its roles and responsibilities (See roles and responsibilities of the Board 3.3). The duty of loyalty requires board members to act in the interest of the company which is often interpreted to mean in the interest of shareholders. This requires the board to act without conflicts of interest. The duty of care requires board members to act on a fully informed basis, with due diligence and in good faith. It is important for boards to demonstrate they act in good faith in order to protect themselves from legal claims since courts accept board decisions if the board: a) follows reasonable process; b) considers all relevant facts; and c) takes decisions in good faith. Good faith is sometimes interpreted to mean how an ordinarily prudent person would behave.

### 3.3. The roles and responsibilities of the Board

*The Goal:* The Board exercises its expected roles.

*Requirements:* The Company Charter is required to describe the basic role of the Board. Some roles defined under best practice are not found in law.



*Recommendations:*

- *Charter and By-laws:* In the event that the Company Charter does not fully describe the roles and responsibilities of the Board under best practice, the By-Laws and/or a board charter should. Such documents should also define what decisions must be approved by the Board.
- *Distinct roles of the Board and Management:* The Company Charter and/or By-laws should articulate the different responsibilities of the Board and Management.
- *Guidance:* The Board should provide objective and thoughtful guidance to Management.
- *Monitoring:* The Board should evaluate the performance of the Company and Management against objectives on a regular basis.
- *Probing:* The Board should probe, question and seek assurances from Management on all matters subject to Board oversight.
- *Intervention:* The Board should not intervene in the management of the Company or arrogate the duly established roles and responsibilities of Management. It should only intervene in management affairs under extraordinary circumstances.
- *Competence and efficacy:* The Board should be competent and efficient in fulfilling its roles and responsibilities.
- *Governance:* The Board should ensure that the Company implements sound governance practices.
- *Accountability:* The Board should be fully accountable to Shareholders.
- *Evaluation:* The Board should consider the extent to which it exercises its expected role in an annual governance evaluation and develop remedial plans as needed (See Corporate governance evaluations 7.0).

*Comments:* Boards have the ultimate responsibility for ensuring that companies achieve their objectives (See Company objectives 1.0) and are fully accountable to shareholders (See Shareholder rights and the role of other Stakeholders 2.0). A board can be expected to, at a minimum, fulfil the following roles and responsibilities:

- Provide leadership
- Set strategic objectives
- Oversee management's implementation of strategic objectives
- Ensure a formal and transparent board member nomination process
- Appoint and/or replace the CEO (and possibly other senior executives) and CEO and key management succession planning
- Incentivise and monitor management and approve executive remuneration
- Oversee communications with Shareholders and protect the company's reputation
- Approve plans, operating budgets, major expenditures and monitor results
- Recommend dividends to the GSM
- Oversee corporate reporting, the integrity of the control environment, the independent audit, the internal audit, risk management and compliance
- Approve risk appetite
- Monitor and manage potential conflicts of interest and related-party transactions
- Regularly assess and improve the company's governance practices
- Take into account the interests of employees and other stakeholders and the goals of Sustainable Development

### 3.4. Board composition

*The Goal:* The Board has the competencies, experience, independence and diversity necessary to fulfil its duties, roles and responsibilities.

*Requirements:* There are no specific requirements under law regarding competencies, experience or diversity of Board Members. However, the law does specify independence requirements (See Independence 3.5) and that Board Members be “fit and proper” for the role (See Fit and proper testing 3.6).

*Recommendations:*

- *Evaluation:* The Board should regularly evaluate its composition in order to identify its human resource needs.
- *Company needs:* The composition and skills on the Board should respond to the Company’s needs, its size and complexity of its operations.
- *Profiles:* The Board should develop written Board Member profile(s) and update them regularly. These profiles should guide the search for future Board Members.
- *Merit:* Board Member appointments should be made based on merit and fulfilment of specific criteria.
- *Diversity Policy:* The Board should establish a Diversity Policy that describes how it intends to achieve the positive impact of diversity, in all respects, both for the Board and Management.
- *Gender:* The Board should be composed to at least 40% of each gender.
- *Evaluation:* The Board should consider the extent to which it exercises its expected role in an annual governance evaluation and develop remedial plans as needed (See Corporate governance evaluations 7.0).
- *Disclosure:* The Company should disclose sufficient information on Board Members so that Shareholders can be reassured as to their competence, experience and likely effectiveness (See Board composition 3.4 and Non-financial reporting and governance reporting 5.3).

*Comments:* Competencies define the requirements for success on the job. Competencies can be thought of as comprising three facets: skills, knowledge and abilities. Most boards will want to have access to a combination of the following competencies though not every board member will have all of them:

- |  |   |
|--|---|
| • Leadership skills                          | • Industry-specific knowledge                               |
| • Decision making skills                     | • Knowledge of innovation and technology                    |
| • Management experience and skills           | • Knowledge of good governance practices                    |
| • Knowledge of operations management         | • Stakeholder and sustainability issues                     |
| • Understanding of accounting and finance    | • Crisis management and restructuring skills                |
| • Capacity for communications                | • Familiarity with international practices and perspectives |
| • Knowledge of audit and control environment |   |

Regarding diversity, a combination of demographic, race, age, gender, educational and professional backgrounds can provide a range of perspectives and insights that contribute to good decision making. A diversity policy can guide a company in its board member selection. The purpose of a diversity policy is to: a) promote the inclusion of different perspectives and ideas; b) mitigate “groupthink” and ensure

that companies have the opportunity to benefit from all available talent; c) make better business decisions; and d) encourage better corporate governance. A diversity policy can be a simple statement posted on the company website that indicates that the company values the benefits of diversity.

### 3.5. Independence

*The Goal:* The Board is objective and fair, and acts independently of special interests and Management in the best interests of the Company and all of its Shareholders.

*Requirements:* The law specifies that one-third of the Board must be independent and defines who cannot be considered independent. The law gives the Company the right to establish additional requirements for independence in the Company Charter. The law also requires an annual evaluation of the independence of the Company's governing bodies which must be disclosed in an Annual Corporate Governance Report. Furthermore, the roles of Chair and CEO are separated by law.

*Recommendations:*

- *Independent Board leadership:* In the event that the Company has a unitary Board, the positions of CEO and Chair should be separated or the Board should have a lead independent board member who can provide a counterbalance to executives and encourage greater independence of mind on the Board.
- *Independence of mind:* All Board Members should act with independence of mind in an unbiased fashion and in the general interest of the Company and all of its Shareholders. This also applies to Board Members who are elected by a special interest.
- *Percentage independents:* The Board should be composed to 50% of independent Board Members.
- *Conflicts of interest:* Any Board Member with a conflict of interest should recuse themselves from Board discussions and decision-making (See 6.7 Conflict of Interest Policy and Related-party Transaction Policy).
- *Training:* The training of Board Members should cover the issue of independence and the obligation of Board Members to act with independence of mind.
- *Disclosure:* Board candidates should report all interests, positions, associations and relationships effecting their independence to the Company as part of the nominations and appointment process (See Nominations and appointments 3.7). The Company should disclose in the Annual Corporate Governance Report: a) the names of Board Members whom it considers independent; b) any factors that might impinge on their independence; and c) whether the Company applies the definition of independence under law and any additional requirements it might have.

*Comments:* A board member can be considered independent if they are free of any interest, position, association or relationship that might influence, or reasonably be perceived to influence, in a material respect, their capacity to bring independent judgement to bear on issues before the board and to act in accordance with their fiduciary duties (See the fiduciary duties of the Board 3.2) to the company and its shareholders. Supervisory boards in Ukraine are composed wholly of non-executives which helps establish some level of independence from management. Yet, even non-executive board members may find their independence threatened if they have links to special interests. A special interest can be defined as an individual or group with the goal of advancing their specific agenda that may conflict with the general interests of shareholders. Ensuring independent thinking may pose additional challenges on

unitary boards that combine executives and non-executives. Unitary boards often appoint lead board members to counterbalance executives, in particular, where the roles of CEO and Chair are combined. Such lead board members may be given special responsibilities for oversight of the company's governance practices, related party transactions, remuneration policies and other areas where there is a heightened potential for conflict of interest amongst executives.

### 3.6. Fit and proper testing

*The Goal:* Board Members have an impeccable reputation and the knowledge, skills and experience to effectively support to the role of the Board.

*Requirements:* The law contains prohibitions against individuals who must not be Board Members such as individuals with a criminal record. The law does not specifically require testing to take place.

*Recommendations:*

- *Testing:* The Board should undertake appropriate checks before appointing or putting forward to Shareholders a candidate for election as a Board Member. Such checks should include due diligence of the candidate's integrity, conflicts of interest, competence, skills and experience.
- *Disclosure:* The Board should disclose all material information in its possession relevant to a decision on whether or not to elect or re-elect a Board Member.

*Comments:* A fit-and-proper- test is a test aimed at preventing corrupt or untrustworthy people from serving on boards. Often, a nominations committee arranges the process of fit and proper testing for board members. It may outsource the task to an external expert or conduct the testing itself. A nominations committee may also arrange the process of disclosure on board members. In companies where there is no nomination committee, this task would fall to the full board.

### 3.7. Nominations and appointments

*The Goal:* The nominations and appointment process is fair, formal, open and transparent.

*Requirements:* There are no legal requirements that specify the process for identifying Board candidates for election. Members of the Board are elected by Shareholders during the GSM for a term not exceeding three years. Board Members can be re-elected an unlimited number of times.

*Recommendations:*

- *Board candidates:* The Board should identify candidates that meet the Company's needs (See Board composition 3.4) relying, where appropriate, on external advisors and/or an open search process.
- *Re-election:* Despite the legal right to re-elect Board Members an unlimited number of times, the Board should ensure that there is adequate refreshment of Board Members so that the Board does not become stagnant.
- *Succession planning:* The Board should plan ahead and be aware of when Boards seats become vacant. The Board should maintain a list of potential candidates.
- *Shareholder proposals:* The Board should ensure that Shareholders have the ability to suggest candidates.

- *Process:* The Board should have a formal process for nominating and electing Board Members and should ensure that the process is respected. Such process should be laid out in the Charter, By-laws or board charter.
- *Proxy voting materials:* The Company should provide Shareholders with proxy voting materials in order to participate in absentia (See General Shareholders Meetings 2.2).
- *Disclosure:* The Board should ensure the disclosure of sufficient information on Board candidates in the proxy voting materials and on the Company website with the notice for the GSM (See General Shareholders Meetings 2.2) to assess the abilities and suitability of each candidate.

*Comments:* The ability to propose and vote on board members is a basic shareholder right (See Shareholder rights 2.1). The board plays a central role in: a) protecting this shareholder right; b) finding appropriate candidates for the board; and c) ensuring a fair and transparent voting process. In many companies, this role is played by a nominations committee which helps professionalise the nominations process (See Board committees 3.11). It is uncommon for jurisdictions to limit the number of re-elections of board members, however, shareholders are wary of entrenched boards and companies may find it advisable to ensure continual refreshment of the board.

### 3.8. Training

#### *Induction training*

*The Goal:* Board Members are sufficiently informed regarding their fiduciary duties, their roles, good governance practices and the nature and strategic challenges of the Company as soon as they take up their posts.

*Requirements:* There is no legal requirement for induction training.

#### *Recommendations:*

- *Induction:* All Board Members should receive induction training upon joining the Board.
- *Content:* The content of induction training should include: a) duties, roles and responsibilities of Board Members; b) independence and independence of mind; c) Board procedures; d) meeting expectations; e) liability issues; f) strategy, structure and operations; g) policies including ethics, conflict of interest and anti-corruption; h) reporting and control environment including internal and external audit; i) governance including the role of committees; j) current issues; and mentoring among others. Induction should include developing a sound understanding of the Company and its operating environment and should therefore include meetings with key executives and visits to Company facilities.
- *Shareholder consultation:* Board Members should seek the views of major Shareholders as well as those of minority Shareholders and Stakeholders as part of the process of familiarising themselves with the Company.

*Comments:* Induction training is arranged and paid for by companies. The induction procedure may be the responsibility of a Corporate Secretary or another officer of the company. In some cases, it may be useful to complement induction training with training provided by an institute of directors. This training would usually be at the expense of the company.

### Ongoing training

*The Goal:* Board Members have up-to-date knowledge and skills to help them contribute effectively to the fulfilment of their roles.

*Requirements:* There are no legal requirements for ongoing training of Board Members.

*Recommendations:*

- *Needs assessment:* The Board should review whether Board Members have the skills and knowledge to effectively fulfil their responsibilities (See Corporate governance evaluations 7.0).
- *Provision of training:* Board Members should have the opportunity to refresh their skills and knowledge in the event that needs are identified.
- *Training plan:* In the event that there are significant gaps, the Board should establish a training plan that specifies what training should be undertaken.

*Comments:* Topics that are of interest may include:

- Industry trends, the state of the competition and international benchmarks
- Technology and innovation
- Sustainability
- Environmental and social risk management
- Corporate social responsibility
- Good governance practices
- Law and legal developments
- Compliance
- Preventing corruption
- Finance and accounting
- The role of the internal audit function versus internal control
- Risk management

Ongoing training can be an important tool to help a company build and maintain a well-informed and effective board. In practice though, most board members tend to learn through hands-on experience. This does not negate the utility of training. Training does, however, have its limits. It costs money, time and effort and can take time to bear results. In the event that there are grave deficiencies in the capacities of board members, it may be more effective to find better candidates through the nominations and appointment process (See Board composition 3.4 and Nominations and appointments 3.7). The base assumption is that, upon appointment, board members are already fully qualified to exercise their roles and that ongoing training is a supplement to help strengthen their existing capacities.

### 3.9. The Board Chair

*The Goal:* The Board has effective leadership.

*Requirements:* The Board must elect the Board Chair who is responsible for organising the Board's work. A member of the Board who worked in Management (whether as a Chair of a formally constituted "management board" or as a CEO) during the previous year may not be elected as the Chair of the Board. The Board is entitled to re-elect the Board Chair at any time.

*Recommendations:*

- *Leadership*: The Chair should have experience, competencies and strong leadership skills to maximise the contribution of each individual Board Member. The Chair should encourage and maintain effective working relationships between the Board and the CEO and Management.
- *Independence*: The Board Chair should be independent. In a unitary Board, the roles of CEO and Chair should be separated or, alternatively, there should be a lead independent board member (See Independence 3.5).
- *Distinction from Management*: Clear distinctions should be drawn between the responsibilities and duties of the Chair and those of the CEO and Management. These distinctions should be captured in the Company Charter and/or By-laws. Neither the Chair nor the Board should encroach on the roles and responsibilities of Management.
- *Board function*: The Chair should ensure that the Board operates effectively. The Chair is responsible for planning Board meetings in advance, setting the agenda, and adhering to high standards of corporate governance.
- *Information*: The Chair is responsible for ensuring that the Board Members receive sufficient, accurate, clear and timely information on all matters under the Board's responsibility.
- *Discussion*: The Chair should encourage and promote critical discussion and ensure that dissenting views can be freely expressed and discussed.
- *Shareholder access*: The Chair should provide Shareholders (particularly larger institutional investors who may expect to have direct contact with the Chair) an opportunity for occasional appropriate dialogue.
- *Corporate Secretary*: The Chair should ensure that the Company has a Corporate Secretary to provide administrative support to the Board (See Corporate Secretary 3.10).
- *Documentation*: The Company Charter, the By-laws or a board charter should refer to and explain the role of the Chair.

*Comments*: The Chair leads the board and ensures that other board members contribute effectively. This can be a difficult role that requires leadership skills and a significant time commitment. It is unlikely that a board member could be the Chair of more than one company at a time. With respect to the independence of the Chair, it is essential that the Chair not show any bias in their leadership. The Chair can be expected to be independent not only from management but also from any special interest or significant shareholder group. Where the roles of CEO and Chair are combined in a unitary board, the appointment of a lead independent director with special oversight responsibilities in areas where there is a heightened potential for conflict of interest amongst executives has become increasingly common. The Chair's fiduciary duty is to act equitably to all shareholders.

### 3.10. The Corporate Secretary

*The Goal*: The Board has the administrative support it requires and access to expert advice on governance and compliance matters so as to be able to effectively fulfil its responsibilities.

*Requirements*: The Board, on the proposal of the Chair, has the right to appoint a Corporate Secretary. Under Ukrainian law, the Corporate Secretary may be a Board Member.

*Recommendations*:

- *Corporate Secretary*: The Company should have a Corporate Secretary.
- *Board member secretaries*: Though law permits it, the Corporate Secretary should not be a Board Member.



- *Combination of roles:* In cases where a separate Corporate Secretary is not feasible, the Company should combine the post with another existing one such as, for example, that of the Legal Counsel.
- *Appointment:* The decision to appoint or remove the Corporate Secretary should be made by or approved by the Board.

*Comments:* Despite the name, the role of the Corporate Secretary is not clerical or secretarial. The importance of the Corporate Secretary has increased over the years. A Corporate Secretary is often neither part of top management nor a member of the board. The trend is for the Corporate Secretary to go beyond providing administrative support to being an advisor with expertise in matters of law, governance and compliance. The role of the Corporate Secretary includes: a) advising the board on legal requirements and good governance practices; b) ensuring that law and board policies and procedures are followed; c) ensuring the timely completion and despatch of board and committee papers; d) maintaining accurate minutes and records; e) organising induction training and professional development for Board Members (See Training 3.8); f) facilitating communications between the board, management and shareholders including being a first point of contact for investor governance concerns; g) assisting in corporate governance evaluations (See Corporate governance evaluations 7.0); and h) helping develop company policies on conflicts of interest and whistleblowing, etc.

### 3.11. Board committees

*The Goal:* The Board has the committee support it needs to optimally fulfil its roles and responsibilities.

*Requirements:* Listed companies are required to have audit, nominations and remuneration committees. Other committees are voluntary.

*Recommendations:*

- *Constitution:* The Board should constitute committees as required by law or when it feels that the quality of its work could thereby be enhanced.
- *Committee charters:* All Board committees should have their own charter. Those charters should cover at least: a) committee objectives; b) authorities and responsibilities; c) chair and composition; and d) meeting frequency and quorum requirements.
- *Disclosure:* The committee charter, the committee's composition, qualifications of committee members, and frequency of meetings should be disclosed in the Company's Annual Corporate Governance Report (See Non-financial reporting and governance reporting 5.3). This information should be available on the Company's website.

*Comments:* The reasons for creating committees of the board include to: a) divide up the work of the Board to make it more manageable i.e. to free up the board's agenda; b) concentrate expertise, permit greater insight into technical issues and devote more time to technical matters; c) give a higher profile to an issue that is considered of great importance to a company; and d) ensure independence and objectivity in certain discussions and decisions where there is potential for conflict of interest or bias. The most common committees amongst listed companies are the audit, nominations and remuneration committees. These three committees, in particular, are expected to have the capacity to arrive at objective and independent decisions because each covers issues where there is a potential conflict of interest between shareholders and management. Committees can be expected to have a minimum of three members. Any less would diminish the quality of their dialogue. In some cases, boards may be too



small to have multiple committees. Companies may find it in their interest to combine committees (such as nominations and remuneration) though the audit committee is generally not combined. Companies may constitute other committees covering topics such as: a) strategy; b) risk; c) governance; and/or d) ethics but are generally not advised to constitute an excessive number of committees because managing the relationship between the full board and the committee requires experience. Companies may find it useful to distinguish between: a) standing committees; and b) ad hoc committees/task forces, or working groups. A standing committee is a permanent committee that meets regularly. The others are structures that may meet intermittently or respond to a punctual need. It is important to recognise that the decisions of a board cannot be delegated to committees. Committees can only prepare decisions that are ultimately adopted by and under the responsibility of the full board.

### *The Audit Committee*

*The Goal:* The control environment of the Company is subject to effective independent oversight such that Stakeholders have assurances that the Company has reliable controls and reporting.

*Requirements:* Listed companies are legally required to have an audit committee. A majority of its members and its chair must be independent Board Members.

### *Recommendations:*

- *Independence:* The audit committee should be composed exclusively of independent Board Members.
- *Knowledge:* Members should collectively have relevant financial knowledge, industry experience and experience with accounting, audit, control and risk management.
- *Combination:* The audit committee should not be combined with other committees.

*Comments:* The full board has the ultimate responsibility for overseeing a company's disclosure (See Roles and responsibilities of the Board 3.3 and Disclosure and transparency 5.0) and its control environment (See Control environment and ethical standards 6.0). However, the audit committee brings special expertise and insight into reporting and control issues. It has the role of:

- Retaining the external auditor
- Ensuring the quality of the external audit
- Ensuring that the independence of the external auditor is not compromised
- Evaluating the effectiveness of the external audit
- Ensuring that the internal auditor has the capacity to work freely, independently and objectively
- Overseeing the efficacy of systems of control, risk management, compliance and internal audit
- Ensuring that financial reports comply with relevant accounting standards and provide a "true and fair view" of the financial position and performance of the company
- Communicating effectively with Shareholders and the markets<sup>8</sup>
- Assisting a board in discharging any other duties related to reporting and control

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<sup>8</sup> Reference is made in the Code to "the markets". The markets—or the marketplace—is where the trading of securities occurs. The markets contain not just existing shareholders of a company but also all other potential buyers and sellers. Thus, communicating effectively with the markets refers not just to communicating with shareholders but also all potential buyers and sellers of a company's securities.

The roles and responsibilities of an audit committee are significant and complex. Audit committee members can typically expect to devote twice the amount of time to their tasks as other board members. It may, as a consequence, not be advisable for the chair of the board or other committee chairs to simultaneously exercise the role of chair of the audit committee. The UCGA/NSSMC provide detailed guidance on the function of audit committees in a supplement to the Code.

#### *The Nominations Committee*

*The Goal:* The Company has the best possible human resources available to staff its Board and Management and is able to ensure stable leadership through effective human resource management and succession planning.

*Requirements:* Listed companies are legally required to have a nominations committee. A majority of members and the Chair must be independent Board Members. The Nominations Committee may be merged with the Remuneration Committee.

#### *Recommendations:*

- *Independence:* The Nominations Committee should be composed wholly of independent Board Members.
- *Knowledge:* The Nominations Committee should have members who have knowledge of human resource management and techniques for conducting searches for Board and Management talent.
- *Disclosure:* The nominations process should be transparent to Shareholders and the markets.

*Comments:* The purpose of a nominations committee is to ensure that the Board has the best possible composition (See Board composition 3.4) and a fair, formal, open and transparent nominations and appointment process (See Nominations and appointments 3.7) that enables a Board to discharge its roles and responsibilities (See The roles and responsibilities of the Board 3.3). A nominations committee may also consider issues of board member and CEO succession, training (See Training 3.8), and corporate governance evaluations (See Corporate governance evaluations 7.0). The UCGA/NSSMC provide detailed guidance on the function of a nominations committee in a supplement to this Code.

#### *The Remuneration Committee*

*The Goal:* The Company has remuneration practices that are fair and help attract and retain the human talent it needs for its Board and Management. Management and staff are incentivised to achieve the Company's objectives and the Company recognises its Management and staff for good performance. The Company is accountable to Shareholders for its remuneration practices.

*Requirements:* Listed companies are legally required to have a Remuneration Committee. A majority of committee members and the committee Chair must be independent. The Remuneration Committee may be merged with the Nominations Committee.

#### *Recommendations:*

- *Independence:* The Remuneration Committee should be composed wholly of independent Board Members.

- *Knowledge:* The members of the committee should have sufficient knowledge of remuneration and incentive compensation practices to effectively fulfil their responsibilities.

*Comments:* Remuneration committees help ensure the thorough and independent preparation of matters relating to the remuneration of management and staff (See Remuneration 3.12). It is the task of a remuneration committee to ensure that incentives are in place for management and staff and that they are appropriately recognised for their contributions to the company. Sometimes, remuneration committees are also responsible for recommending the remuneration and benefits due to board members. This may pose a conflict of interest. As a consequence, some boards rely on independent external advisors to help them set the remuneration and benefits of board members. Another way companies address this conflict of interest is through the full disclosure of board member remuneration (See Non-financial reporting 5.3). The UCGA/NSSMC provide detailed guidance on the function of remuneration committees in a supplement to the Code.

### 3.12. Remuneration

*The Goal:* The remuneration of Board Members and Management is transparent, fair and sufficient to attract, motivate and retain talent.

*Requirements:* The law requires a Remuneration Policy for Management approved by the Board and a Remuneration Policy for Board Members approved by the GSM which must be disclosed on the Company website. There is also a requirement to draw up and disclose an annual Remuneration Report.

*Recommendations:*

- *Pay levels:* The remuneration of Board Members and Management should be sufficient to attract the needed profiles but should not be excessive.
- *Link to performance:* For Management, there should be a link between their pay and the overall performance of the Company as well as their fulfilment of individual performance objectives.
- *Types of remuneration:* Board Member remuneration should be composed exclusively of meeting attendance fees and/or retainers and should not include any significant option or equity component.
- *Independence:* Decisions on the remuneration of top Management should be objective and independent and free from improper influence by Management. The remuneration levels of Management and Board Members should be set with the assistance of independent external expert advisors.
- *Say on pay:* Shareholders should be able to make their views known on the Remuneration Policy and the remuneration of Board Members and Management at the GSM. The Remuneration Policy for Board Members and Management must be approved by Shareholders at the GSM. The equity component of compensation schemes should be subject to Shareholder approval.
- *Disclosure:* The Company should, at a minimum, disclose the aggregate remuneration for the Board as well as the aggregate remuneration of the top 5 paid members of Management. The Company should disclose the link between pay-outs and Key Performance Indicators (KPIs) as well as any key decisions taken by the Remuneration Committee in the given year.

*Comments:* Remuneration policies are intended to encourage the convergence of the financial interests of management and shareholders. They may establish types of performance-related remuneration including share options, bonus programmes and define the link between pay and company

performance. Performance-related remuneration is sometimes subject to an absolute limit. Although establishing precise board and executive pay levels is not typically a responsibility for a GSM, it is increasingly common for shareholders to have the opportunity to express their views on remuneration. It is considered good practice for remuneration issues to be handled by a remuneration committee (See Board committees 3.11) composed of at least a majority of independent members.

### 3.13. Board size

*The Goal:* The Board has a size that supports the fulfilment of its roles and responsibilities and its composition goals.

*Requirements:* Law requires a minimum Board size of 5. No maximum Board size is specified.

*Recommendations:*

- *Minimum:* The Board should have a minimum of 7 members.
- *Maximum:* While there is no fixed maximum, the Company should avoid having excessively large Boards.

*Comments:* There is no agreement on the optimum size of a board. Different studies show different sizes in different countries. Boards in some countries range from as few as 3 members to more than 30. Board sizes may also vary depending upon the industry, the stage of development of the company and other contextual issues. The average board size in both the EU and US is approximately 9 members. Since boards may be required to have an audit committee and a remuneration committee (possibly combined with a nominations committee), the minimum board size would be 6 if there is no overlap in committee membership and if the minimum committee size is 3. If, in addition, the board has a Chair that is not simultaneously a committee member, and there is no overlap in committee membership, then the minimum board size rises to 7. Five board members can be considered sufficient for smaller companies. Additional committees and diversity goals may make additional board members necessary. Empirical data does not indicate any clear maximum though anecdotal evidence suggests that boards become unwieldy with size.

## 4. Co-operation between Management and the Board

*The Goal:* The Company has effective Management that is accountable to both the Board and Shareholders for the achievement of Company objectives. The Board and Management have distinct roles and responsibilities. They collaborate effectively to the benefit of the Company and do not infringe on each other's roles or responsibilities.

*Requirements:* The basic parameters of the interaction between Management and the Board are set down in Company Law. Management is responsible for the day-to-day management of the Company and for implementing Board and GSM decisions. Management's responsibilities exclude any matters under the exclusive competence of the GSM and/or the Board.

*Recommendations:*

- *Roles and responsibilities:* The Company Charter and/or By-laws should articulate the different roles and responsibilities of the Board and Management. (The roles and responsibilities of the Board are described in 3.3 above.) Management should be responsible for the daily operations

of the Company, staffing, goal setting, administering, delegating, enforcing policy, and so on under the supervision of the Board.

- *Dialogue:* An open and constructive dialogue should exist between Management and the Board.
- *Strategy:* Management should develop and implement the Company strategy under the supervision of the Board. The Company strategy should be subject to Board approval. Management should have full operational autonomy to manage the Company on the basis of the approved strategy and to achieve the defined objectives.
- *Guidance:* The Board should advise and supervise Management and approve all decisions of fundamental importance as defined in the Charter and By-law. Management should actively seek the feedback and guidance of the Board on all major corporate issues in order to ensure that issues are jointly considered and resolved.
- *Key Performance Indicators (KPIs):* Management should use KPIs to track their progress in achieving the Company strategy. Such KPIs should be selected with the approval of the Board.
- *Reporting:* Management should regularly report to the Board on its progress in achieving the Company strategy and KPIs. It should also report on all other issues relevant to the work of the Board (See the roles and responsibilities of the Board 3.3).
- *Timeliness:* All information relevant to the Board's responsibilities should be provided to the Board at least one week before Board meetings.
- *Material events:* Management should inform the Chair of the Board immediately of any material events that may have arisen between Board meetings.
- *Governance culture:* Management should actively promote good governance practices and a good governance culture.
- *Disclosure:* The Company should disclose what matters are expressly reserved to the Board and those delegated to Management.

*Comments:* The term “management” is used to describe the leadership positions in a company who are responsible for achieving the company’s strategic objectives. For some companies management is a loosely defined group. Others may define a top management team that might include the CEO, CFO, COO and possibly some additional managers such as a head of marketing or a chief technology officer. Others still may constitute a formal management board with a charter that sets down roles and responsibilities, frequency of meetings, voting procedures, quorum requirements and so on. The Code does not favour any particular arrangement and, given the variety of practice in Ukraine, each of these groupings is simply referred to as “Management”. The board approves the company strategy and oversees management which is responsible for the implementation of the strategy and the day-to-day operations of the company. In practice, virtually all companies strike a different balance between oversight and management and sometimes striking the right balance is challenging. In some cases, boards are obtrusive and excessively operational. In other cases, they may be unassertive or uninvolved. In organisations with good governance practices, both the board and management are well-informed of their distinct roles and respect these roles and co-operate actively in the achievement of company objectives. The Chair and the CEO play an essential role in ensuring that both boards and management observe their proper roles. They need to respect each other and be able to work together closely as a team. The Chair needs to be well-versed in good governance practices and sensitive to the dynamics between the board and management. The CEO is head of management and the main interface between the management and the board. The CEO leads the development of the company’s strategy, leads the

other members of management and evaluates their work, and communicates on behalf of the company with all of the company's stakeholders. The CEO needs to be able to work with the Chair and the board as a trusted partner.

## 5. Disclosure and transparency

### 5.1. Communications with Shareholders

*The Goal:* The Shareholders and the markets have timely and fair access to all information that is material to their investment decisions and such information is presented in a balanced fashion.

*Requirements:* The Company should disclose all material information that could reasonably be expected to have an effect on the Company share price or stewardship decisions to Shareholders and the markets and should do so as soon as it becomes available. Disclosure should be made to all Shareholders and the markets simultaneously in order to prevent unfair trading advantages.

*Recommendations:*

- *Policies:* The Company should have a written Disclosure Policy that describes what information the Company will disclose and how it intends to communicate with Shareholders and the markets.
- *Disclosure:* The Disclosure Policy should be available on the Company website.
- *Balance:* The Company's disclosures should present a balanced view and cover both positive and negative information.

*Comments:* The purpose of a disclosure policy is to raise awareness among board members, management, employees, shareholders and the markets of the company's approach to disclosure. A disclosure policy can include:

- Role of Board in overseeing disclosure
- Types of disclosure required including: a) financial; b) environmental c) social; and/or d) sustainability
- Interaction of company with the investment community
- Interactions with analysts and analysts' meetings
- Designation of an official company spokesperson
- Use of company website for disclosure
- Principles of disclosure such as: a) timing; b) omission; c) unfavourable information; d) selective disclosure; e) inadvertent disclosure; f) corrections.
- Definition of materiality
- Forward-looking information
- Requirement to report progress against KPIs at least annually
- Treatment of confidential information
- Prohibition on discussing company on social networks

In order to reduce documentation requirements, it is possible to combine a company's Disclosure Policy with its Shareholder Engagement Policy (See Company engagement with Shareholders 2.3). The NSSMC and UCGA plan to develop a model Disclosure Policy as part of their future work on Model Policies and Documents.

## 5.2. Financial reporting

*The Goal:* Information on the financial performance and position of the Company is objective, reliable and clear and Shareholders are satisfied that they have sufficient information to inform their investment decisions.

*Requirements:* Companies must prepare and present their financial statements to shareholders for approval at the GSM. For Public Interest Entities (PIEs),<sup>9</sup> the financial statements must be prepared in accordance with International Financial Reporting Standards (IFRS). For other companies, the financial statements must be prepared according to Ukrainian GAAP. The Annual Report must contain a report by management (Management Discussion and Analysis—MD&A). The Company must make its Annual Report public within 4 months of the end of the financial year and the Annual Report must be posted on the Company website. Management must certify to the Board that the financial statements of the Company provide a true and fair view, comply with accounting standards and that systems of internal control and risk management are sound before the Board approves the reports.

*Recommendations:*

- *Reporting standards:* The Board should oversee Management in its production of financial reports and ensure that the Company produces its financial reports in accordance with applicable law and financial reporting standards.
- *Content:* The Annual Report should contain the elements of a best practice report as described in the Comments below.

*Comments:* Financial reporting and the annual report are, arguably, the central elements of corporate communications. A best practice annual report would typically include the following:

- General information about the company
- Letter to the shareholders from the Chair or the board
- Letter to the shareholders from the CEO
- Management’s discussion and analysis (MD&A)
- Operating and financial highlights
- Narrative text, graphics and photos
- Financial statements including: a) statement of financial position (balance sheet); b) income statement (profit and loss statement); c) statement of changes in equity; d) cash flow statement; e) notes to the financial statements; and f) accounting policies
- The auditor’s report and opinion

## 5.3. Non-financial reporting

*The Goal:* Relevant non-financial Information, including on the governance of the Company, is provided to Shareholders and the markets to better inform their investment decisions. The impact of the Company on society and the environment is made clear to stakeholders.

*Requirements:* Companies must disclose an Annual Corporate Governance Report as part of the Annual Report. Separate social and environmental reporting is not required. The Board must sign off on the

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<sup>9</sup> A Public Interest Entity (PIE) under European Union law is any entity listed on a regulated market, credit and insurance institutions whether listed or not, and other entities designated of public interest by the state.



Annual Corporate Governance Report separately from its financial statements prior to the approval by the GSM.

*Recommendations:*

- *Disclosure standards:* Non-financial reporting should be done in accordance with relevant national and/or international standards.
- *Governance reporting:* Governance reporting should cover all of the issues listed in this Code.
- *Environmental and social reporting:* The Company should report on its societal and environmental impact (See the role of other Stakeholders 2.5 and Sustainable Development 2.6).

*Comments:* There are many types of non-financial disclosure. Some are designed to support a better understanding of the company's financial reports. Others, such as corporate governance reporting, are designed to help understand practices that influence the companies risk and performance. Others still, such as environmental and social reporting, are intended to describe the role of the company in society. Each of these forms of reporting (financial, governance, and social and environmental) are subject to disclosure standards. Financial reporting standards are covered in 5.2 above. With respect to governance reporting, UNCTAD publishes its *Guidance on Good Practices in Corporate Governance Disclosure* which is designed to help companies prepare their governance disclosure. The UNCTAD Guidance is divided into: a) financial disclosures; b) non-financial disclosures; c) general meetings; d) timing and means of disclosure; and e) good practices for compliance. Frequently made non-financial disclosures include the following:

- Company objectives
- Governance structures and policies including charters and by-laws, and policies on conflict of interest, remuneration, dividends, etc.
- Members of the board and key executives and their backgrounds
- Board member and executive remuneration
- Stakeholder and sustainability reporting
- Ownership and shareholder rights
- Material foreseeable risk factors and risk appetite
- Changes in control and transactions in significant assets
- Independence of the external auditors
- The internal audit function
- Material issues regarding stakeholders, stakeholder engagement policy and stakeholder mapping

With respect to the standards that define good environmental and social reporting, companies are usually provided significant flexibility in how to disclose. Various standards exist including the *UN Global Compact*, the *OECD Guidelines for Multinational Enterprises*, ISO 26000 and the standards of the Global Reporting Initiative (GRI). Often, disclosure requirements are applied proportionally, i.e. they take into account the size, complexity and impact of the company. For example, EU law only requires public interest entities with more than 500 employees to disclose information on the way they operate and manage social and environmental challenges. In any event, there is an increasing expectation that boards take an equivalent interest in non-financial disclosure (stakeholder, environmental, social and governance reporting) as they are expected to in company financial statements.



#### 5.4. The independent external audit

*The Goal:* Shareholders, stakeholders and the markets have full confidence in the quality of the Company's financial and non-financial reports.

*Requirements:* For PIEs, the Company's annual financial statement and the Annual Corporate Governance Report must be audited by an independent external auditor. For PIEs, the audit of annual financial statement must be conducted in accordance with International Standards on Auditing (ISA) which require the auditor to form an opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework and to issue their opinion in a written auditor's report. The Board must submit its recommendation for the appointment, reappointment, removal and remuneration of the independent external auditor to Shareholders for approval at the GSM. Non-PIEs are not required to have an annual audit of their financial statements or non-financial reports.

*Recommendations:*

- *Audit standards:* The Board should oversee the independent external audit and ensure that the annual financial reports are audited in accordance with applicable law and audit standards.
- *Capacity:* The Board should verify that the independent external auditor has sufficient capacity, resources and time to carry out an effective audit.
- *Independence:* The Board should establish whether the external auditor is sufficiently independent from the Company, its Management, and its major Shareholders.
- *Disclosure:* The Board's findings regarding the independence of the external auditor should be disclosed in the Annual Report.
- *Rotation:* Companies should rotate the key audit partner in charge of the independent external audit every 7 years and the audit firm every 10 years for listed companies and other Public Interest Entities.
- *Deficiencies:* The Board and Management should pay special attention to the communications of the independent external auditor with respect to control deficiencies in the context of their audit of the financial statements and ensure that such concerns are addressed.

*Comments:* An objective independent examination of a company's financial reports increases their value and investor confidence. This, in turn, has the potential of reducing the company's cost of capital. While independent external audits have traditionally been done on financial statements, they are increasingly being done on non-financial reporting. Regarding mandatory audit firm rotation (MFR), the core requirement in the EU is 10 years MFR for all PIEs with the ability to extend the period for 10 years if a tender is undertaken. While the overall responsibility for ensuring the efficacy and independence of the independent external audit lies with a board, it is generally assisted by an audit committee (See 3.11 Board committees) that bring an independent view and special knowledge to the task of audit oversight.

#### 5.5. Dividends and Dividend Policy

*The Goal:* The dividend policy is clear to Shareholders and the markets.

*Requirements:* There is no obligation to pay dividends or for the Company to have a Dividend Policy. However, the procedure for paying dividends is established by law.

*Recommendations:*

- *Policies:* The Board should develop and submit a Dividend Policy for GSM approval.
- *Disclosure:* The Dividend Policy should be published on the Company's website.

*Comments:* Determining a dividend pay-out is the responsibility of the board. A clear Dividend Policy can help a board decide if and how earnings are paid to shareholders. Dividend Policies can be succinct. They may specify the distribution of some or all of the profits of the company and a target dividend (often expressed as a percentage of earnings or free cash flow). The Dividend Policy might make pay-outs subject to the operating and investment requirements of the company, solvency requirements, and/or loan covenants among others. The timing of dividend payments may also be specified as well as the need for shareholder approval at the GSM. The UCGA/NSSMC plan to publish a sample dividend policy as a supplement to the Code.

## 5.6. The Company website

*The Goal:* All information destined to Shareholders, the markets and other Stakeholders is well-organised and made easily available on the Company website.

*Requirements:* The Company must have an official website for public disclosure of information and disclose on it.

*Recommendations:*

- *Content:* The Company website should provide Stakeholders with all the information to which they have a right and any other information in which they could reasonably be expected to have a significant interest.
- *Governance section:* The website should include a separate section dedicated exclusively to corporate governance.
- *Maintenance:* The governance section of the website should be kept up-to-date. Historical data should be available on the website. Historical data should go back at least several years and, ideally, longer.
- *Language:* The main disclosures such as the Annual Report and the Annual Corporate Governance Report should be disclosed in English in addition to Ukrainian when a significant number of the Company's Shareholders are not native speakers of Ukrainian or where the Company is seeking an international shareholder base.

*Comments:* A reasonably complete website can be expected to include the financial and non-financial information described in 5.2 Financial reporting and 5.3 Non-financial and governance reporting above.

## 6. The control environment and ethical standards<sup>10</sup>

### 6.1. Internal controls

*The Goal:* The system for internal control provide assurances that the Company has adequate controls over operations, financial reporting and compliance matters.

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<sup>10</sup> The control environment is a collection of systems, functions and practices that determine the effectiveness of a company's internal controls. The board, the audit committee and management play a central role in ensuring a sound control environment and are jointly responsible for exercising leadership and influencing attitudes towards control. A sound control environment helps the Company: a) achieve its strategic objectives; b) produce reliable

*Requirements:* An adequate system of internal controls is not required by law.

*Recommendations:*

- *Establishment:* Companies should have an effective system of internal control.
- *Monitoring:* The Audit Committee is expected to review the Company's internal controls with the assistance of the Internal Auditor and the External Auditor at least once a year and ensure corrective action and improvement if required.
- *Standards:* The system of internal control should comply with international standards of best practice.

*Comments:* Internal control is a management function. Internal controls are measures taken to protect a company's assets. They limit the actions of employees by requiring authorisations, approvals and verifications of transactions. They segregate duties so that no one person has unsupervised control over an asset and prevent employees from simultaneously making and recording transactions. Examples of control measures include prohibiting the same person from: a) initiating and recording transactions; b) making purchases and approving payments; c) ordering and accepting inventory; d) approving vendors and making payments; e) receiving bills and approving payments; and f) authorising returns and issuing refunds. In addition, internal controls may comprise: a) monthly reconciliations of bank accounts; b) review and verification of refunds; c) reconciliation of petty cash accounts; d) audits of payroll disbursements; or e) conducting physical inventory. Other measures may include physical security barriers, restrictions on access to records, locks and surveillance equipment. Internal controls also record transactions and create an auditable document trail.

## 6.2. Risk management

*The Goal:* Risk management provides companies and investors a high degree of confidence in their decisions. The process of risk management detects, analyses and controls risks and mitigates possible circumstances that could have a negative impact on achieving company objectives.

*Requirements:* Formal risk oversight is not required by law.

*Recommendations:*

- *Board responsibility:* The Board should have the responsibility for ensuring that an appropriate risk management framework, including risk management policy, is in place.

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financial reports; c) operate efficiently and effectively; d) comply with all applicable laws and regulations; and e) safeguard its assets. This Code reproduces the essential components included in the *Three Lines of Defence Model* endorsed by the Global Institute of Internal Auditors (IIA) (<https://na.theiia.org/>) and the Institute of Directors (IoD) (<https://www.iod.com/>). Under that model, management and internal controls (6.1) are the first line of defence. The second line of defence consists of several components including risk management (6.2) and compliance (6.3). The third line of defence is internal audit (6.4) which provides for independent assurances. The control environment is complemented and strengthened by ethical standards (6.5) anti-corruption (6.6) and conflict of interest and related-party transaction policies (6.7). The independent external auditor (5.4) is not formally part of a company's three lines of defence but plays an important role in the governance and control structure.

- *Independence:* The Audit Committee should establish whether the risk management function is sufficiently independent from the Company, its Management, and any major Shareholders.
- *Risk appetite:* The Board should decide the nature and extent of the risks that the Company is prepared to take to meet its objectives and should formally approve the Company's risk appetite.
- *Implementation:* Management should design and implement the risk management framework based on good international practice and ensure that the company operates within the risk appetite set by the Board.
- *Risk Committee:* The Board should consider establishing a Risk Committee with a majority of independent Board Members to oversee risk.
- *Annual review:* The Board should assure itself annually that its risk management framework is sound.
- *Disclosure:* The Board should disclose annually whether a review of its risk management framework has taken place and, if so, its key conclusions. The Board should disclose an annual statement on its risk appetite and risk tolerance.
- *Sustainability:* The Company should consider and disclose whether it has any material exposure to sustainability or environmental risk. Any such risks should be integrated into the risk management framework. The Board should be aware of the Company's environmental and social risks and oversee their treatment by management.

*Comments:* A "risk management framework" is the structured process of identifying and analysing risks and developing a response. A "risk management policy" provides a plan for managing risk. "Risk appetite" is a higher-level concept that considers the levels of risk that a company deems acceptable, while "risk tolerance" is narrower and sets the acceptable level of variation around objectives. "Sustainability risk" refers to the uncertainty of being able to sustain the growth and/or profitability of a company over time. An example of sustainability risk relates to climate change. Extreme weather and climate change policy can affect the profitability of corporations but there are other risks such as decreasing availability of fossil fuels and water supplies, unsustainable urbanisation, etc. Some companies may wish to locate oversight of the risk management function in the Audit Committee rather than having a standalone Risk Committee.

### 6.3. Compliance

*The Goal:* The Company complies with internal rules, policies and procedures and external law and regulations.

*Requirements:* There is no legal requirement for a company to have a compliance function.

*Recommendations:*

- *Establishment:* The Company should have a formal compliance function.
- *Independence:* The Board should establish whether the compliance function is sufficiently independent from the Company, its Management, and any major Shareholders.
- *Effectiveness:* Management should assist and promote the compliance function while the Board should exercise oversight to ensure that the compliance function is effective.

*Comments:* The compliance function protects companies against risks, combats potential market abuse, protects the company's customers and also prevents money laundering and financing of terrorism. A

compliance function can have a variety of responsibilities including: a) monitoring and detecting compliance issues; b) resolving problems; and c) proposing strategies to prevent future compliance failures. Compliance functions are considered particularly important in banks and other financial institutions because they operate in highly regulated industries with possible systemic consequences of financial institution failure. Larger sophisticated companies, can be expected to have distinct internal control and compliance functions. Smaller enterprises may have them combined. Ideally, a compliance function retains some level of independence from management akin to an internal audit function. It may be advisable for a compliance function to have direct access to the board in a fashion similar to the internal auditor.

#### 6.4. The internal audit function

*The Goal:* The internal audit function provides independent assurances that the Company has in place an effective internal control system, risk management and a compliance function.

*Requirements:* An internal audit function is required by law for listed companies, banks and PIEs with state ownership.

*Recommendations:*

- *Objective:* The internal audit function should provide reasonable assurance that the Company's internal controls are effective and adequate.
- *Scope of work:* The internal audit function should have complete freedom to choose its planned audits using a risk-based approach.
- *Independence:* The Audit Committee should establish whether the internal audit function is sufficiently independent from the Company, its Management, and any major Shareholders.
- *Standards:* The internal audit function should operate under international best practice standards established for internal audit.
- *Reporting line:* the internal audit function should have a direct and unhampered reporting relationship to the Board through the Audit Committee.
- *Authority:* The Board should support the work of the internal audit function, guard their independence and ensure they have the authority to fulfil their responsibilities.
- *Disclosure:* The Company should disclose if it has an internal audit function, its role and its reporting relationships within the Company.

*Comments:* Internal audit is not the same as internal control. Internal control system is an operational function established by management. Internal audit, on the other hand, is a function that operates independently from management and makes decisions independently from management. It is an assurance and consulting service that is primarily directed at evaluating a company's internal control system, components of corporate governance and the risk management and compliance functions. The international reference points for establishing and maintaining effective systems of internal audit and internal control are the Institute of Internal Auditors (IIA) and the Committee of Sponsoring Organizations of the Treadway Commission (COSO).<sup>11,12</sup> An external auditor may review both internal controls and the internal audit function in the context of their external audit. The goal of the external auditor is to verify whether the company's systems can be relied on for the purposes of the external

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<sup>11</sup> Institute of Internal Auditors.

<sup>12</sup> COSO Framework: <https://www.coso.org/>.

audit and ensure that the financial statements give a true and fair view of the company's financial position.

## 6.5. The Ethics Code

*The Goal:* The Company, its Board, Management and staff act ethically and with integrity.

*Requirements:* Companies must comply with the law but there is no requirement for companies to have an Ethics Code or code of conduct.

*Recommendations:*

- *Policies:* The Company should have an Ethics Code. The Ethics Code should apply to and be mandatory for the Board, Management and staff.
- *Leadership:* The Ethics Code should be actively promoted by the Board and Management.
- *Reporting misconduct:* As part of its ethics programme, the Company should permit individuals to report unlawful or unethical behaviour anonymously and securely. The Company should follow up on information in good faith and take appropriate action.
- *Communication:* The Ethics Code should be widely communicated within the Company.
- *Training:* All Board Members, Managers and staff should receive training in the Ethics Code and ethical issues with tailored training being provided to staff in high-risk positions.
- *Guidance:* The Company should have the capacity to provide employees and (where appropriate) business partners guidance on ethical issues.
- *Monitoring:* The Board and Management should monitor and assess the effectiveness of the Ethics Code and propose remedial action where necessary.
- *Disclosure:* The Ethics Code and reports on its implementation and any amendments to the Ethics Code should be disclosed on the Company's website. Should the Ethics Code have been set aside for any particular circumstance in the prior year this should be disclosed and fully explained.

*Comments:* Ethics goes beyond compliance with the law (See Compliance 6.3). Legal standards are based on written law, while ethical standards are based on a broader sense of what is right or wrong. Some actions may be legal but not ethical. Shareholders and other stakeholders expect companies to act not just legally but also ethically. They expect companies to adhere to basic rules of ethical conduct in their treatment of suppliers, customers, employees, government, local communities and the environment. Ethics codes typically require people affiliated with a company to: a) act in the best interest of the company; b) comply with rules and policies; c) avoid conflicts of interest; d) not misuse company assets or take advantage of circumstances for personal gain, and so on. Ethical behaviour is ultimately a matter of culture. A culture of ethics can enhance the reputation of a company and reduce risks. The following items are often covered in ethics codes:

- Purpose, values and principles of the code
- Scope of the code
- Respect at the workplace
- Harassment
- Conflicts of interest
- Gifts from vendors
- Rules regarding the use of company assets
- Use of information and intellectual property
- Confidentiality
- Procurement
- Facilitation payments

- Hospitality, entertainment and expenses
- Health and safety issues
- Human rights and child labour
- Dealing with external stakeholders
- Political and charitable contributions
- Reporting misconduct or violations
- Investigations and corrective/disciplinary actions

Though ethics and conduct codes are not primarily intended to ensure legal compliance, in practice, many reiterate basic legal obligations such as prohibitions against theft, insider trading, self-dealing and abusive related-party transactions. Some ethics codes cover issues such as bribery, corruption, and money-laundering and may, thus, overlap with anti-corruption policies (See Anti-corruption policy 6.6).

### 6.6. Anti-corruption Policy

*The Goal:* The Company does not engage in any corrupt practices and is seen as being honest and law-abiding.

*Requirements:* The law requires state and communal entities and all legal entities who participate in public procurement (where the cost of such contracts are higher than a legally fixed amount) to develop and implement anti-corruption measures. Management and shareholders must ensure the regular assessment of corruption risks. The Criminal Code penalises corrupt acts committed in the interests of a company.

*Recommendations:*

- *Policies:* The Company should have an Anti-corruption Policy.
- *Leadership:* The Board and Management should ensure the effective implementation of the Anti-corruption Policy.
- *Communication:* The Anti-corruption Policy should be widely communicated within the Company.
- *Training:* All Board Members, Managers and staff should receive training in the Anti-corruption Policy.
- *Monitoring:* The Board and Management should monitor and assess the effectiveness of the Anti-corruption Policy and propose remedial actions where necessary.
- *Third parties:* The Company should ensure implementation and oversight of the Anti-corruption Policy in its subsidiaries and affiliates. The Company should inform its Stakeholders including business partners of its Anti-corruption Policy and seek a reciprocal commitment from them.
- *Disclosure:* The Anti-corruption Policy and reports on its implementation should be disclosed on the Company's website.

*Comments:* An anti-corruption policy is designed to ensure that: a) the company and individuals act in accordance with company values; b) protect the company's reputation; c) demonstrate commitment to stakeholders; d) ensure compliance with law; and e) strengthen awareness of anti-bribery measures. A typical anti-corruption policy can be expected to include:

- Purpose and objectives of the anti-corruption policy
- Requirement of company staff to comply
- Dealing with third party representatives
- Record keeping and reporting
- Reporting of breaches of the policy



- Prohibited payments
- Interactions with public officials
- Offering or receiving hospitality from customers, suppliers or others
- Administration of the policy and role of board and management
- Listing of applicable laws and standards
- Forms for employees to acknowledge the policy

While not the same, it is common for ethics codes and anti-corruption policies to contain some overlap. The NSSMC and UCGA plan to develop a model Anti-corruption Policy as part of their future work on Model Policies and Documents.

#### 6.7. Conflicts of Interest Policy and Related-party Transactions Policy

*The Goal:* The Company and its Shareholders are protected from abuses arising from conflicts of interest.

*Requirements:* There is no legal requirement for a company to have a conflict of interest policy though securities exchange regulation prohibits insider trading and self-dealing. Board Members and Management must disclose all equity trades or derivative transactions for their own account in the company's or affiliated securities to the NSSMC within 5 working days of execution. Law requires employees and company officials to notify the company's anti-corruption officer or legal head or shareholder of any actual or potential conflict of interest without delay. The law requires that the Board hire an independent external auditor to check if a related-party transaction takes place under normal market conditions whereupon the Board must approve or reject such transaction.

*Recommendations:*

- *Policies:* The Company should have a Conflict of Interest Policy (or multiple policies) that covers: a) conflicts of interest and their prevention and management; b) related-party transactions; c) insider trading; and d) self-dealing.
- *Monitoring:* The Board should oversee the implementation of the Company's Conflict of Interest Policy and the systems that ensure that conflicts of interest are controlled effectively.
- *Disclosure:* The Conflict of Interest Policy should be disclosed on the Company website. Members of the Board and Management should be required to report to the Board any potential conflict of interest with the Company.

*Comments:* The purpose of a conflict of interest policy is to protect a company's interest when it is contemplating entering into a transaction or arrangement that might benefit the private interest of a board member, a manager or staff member. A conflict of interest occurs when an individual or organisation has multiple interests which could unduly influence their judgment or actions and undermine their ability to work objectively and effectively. Conflicts of interest may be associated with: a) receiving gifts from business partners; b) self-dealing that benefits the individual, family or friends; c) outside employment that conflicts with the interest of the company; or d) family or friends receiving employment or beneficial treatment, amongst others. These are usually addressed by: a) eliminating the conflict by resigning; b) selling stock; c) recusal from decisions; d) disclosure of the conflict; and e) using third-party evaluations to make decisions. A related-party transaction is a transaction where a party with influence over the transaction has a conflict of interest. They are not necessarily bad but are vulnerable to abuse and thus require special oversight by boards. Key



elements of a related-party transaction policy are: a) disclosure of interests; b) disclosure of conflicts of interest; c) avoidance of conflict of interest; d) recusal from decision making; e) arm's-length decision making; f) board approval of transactions; g) disclosure of related-party transactions; and h) cancellation of all unapproved related-party transactions amongst others. A conflict of interest policy can be expected to contain:

- A definition and examples of conflicts of interest
- Scope (persons covered by the policy)
- Transactions covered by the policy
- Remedies including: disclosure, refraining from influence, and recusal
- Procedures for reporting conflicts of interest
- Procedures for approving a covered transaction
- The administration of the policy
- Forms for declaring a conflict of interest

The NSSMC and UCGA plan to develop a model Conflict of Interest and Related-party Transaction Policy as part of their future work on Model Policies and Documents.

## 7. Corporate governance evaluations

*The Goal:* The Company is abreast of trends in good governance and ensures a continuing cycle of improvement in its governance practices.

*Requirements:* The law requires an annual evaluation of the Company's governing bodies, its committees and their members, as well as their independence status. Companies must disclose that governance evaluations have taken place in their Annual Corporate Governance Report.

*Recommendations:*

- *Code compliance:* In addition to the assessment required by law, the annual assessment should consider the Company's compliance with this Code.
- *Performance:* The annual evaluation should include an assessment of the attendance and contributions of individual Board Members.
- *Action plans:* The annual evaluation should result in the establishment of a Board-approved Action Plan that includes goals that aim at improving the Company's corporate governance practices.
- *Monitoring:* The Board should assess progress against the goals set down in the Action Plan annually.
- *External expertise:* An independent external expert should be used every 3 years to enhance the objectivity of the annual evaluation and to contribute their expertise in corporate governance.

*Comments:* In the same manner that top management benefit from an annual evaluation against performance objectives, boards can benefit from evaluation. Board evaluations are increasingly considered best practice and are becoming more common internationally. The benefits of stepping back each year to assess the effectiveness of a board's work are clear. Evaluation serves to identify weaknesses and strengthen the boards and companies. Regular assessment against a benchmark is also necessary to establish a baseline from which to measure progress and to develop action plans for future improvement. Board evaluations are inevitably challenging for board members. The evaluation process can be made easier, however, by: a) using facilitators; b) keeping the results confidential; and c) by

treating the evaluation as a forward-looking process whose goal is the improvement of the board's work rather than finding fault and assigning blame. Board evaluations can be either self-evaluations, external evaluations (done by an independent expert) or assisted self-evaluations. Most companies tend to prefer to conduct self-evaluations or assisted self-evaluations so that they can better control the process. External facilitators are useful in bringing governance expertise to the company and enhancing the objectivity of evaluations.

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