


International Financial Accounting and Policy


Corporate Governance

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A close-up photograph of a hand holding a golden key. The hand is positioned on the left side of the frame, with the thumb and index finger gripping the key's head. The key is held horizontally, pointing towards the right. The background is a dark blue gradient.A close-up photograph of a hand holding a golden key, similar to the one in the first slide. The hand is positioned on the left side of the frame, with the thumb and index finger gripping the key's head. The key is held horizontally, pointing towards the right. The background is a dark blue gradient.


Corporate Governance

- Ø What is CG?
 - Ø Corporate governance is the system by which companies are directed and controlled.
- Ø Why is CG important?
 - Ø Owners of a company and the people who manage the company are not always the same (Trust).
 - Ø To ensure that the interest of all stakeholders are safeguarded.
 - Ø If there are good CG practices available, there will be strong controls and control environment and it would be a well managed business, so audit risk will be minimal thereby can reduce the NET of audit procedures.




OECD Principles of CG

OECD Principles of Corporate Governance	
I	The corporate governance framework should promote transparent and efficient markets, be consistent with the rule of law and clearly articulate the division of responsibilities among different supervisory, regulatory and enforcement authorities.
II	The corporate governance framework should protect and facilitate the exercise of shareholders' rights.
III	The corporate governance framework should ensure the equitable treatment of all shareholders, including minority and foreign shareholders. All shareholders should have the opportunity to obtain effective redress for violation of their rights.
IV	The corporate governance framework should recognise the rights of stakeholders established by law or through mutual agreements and encourage active co-operation between corporations and stakeholders in creating wealth, jobs and the sustainability of financially sound enterprises.
V	The corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, ownership and governance of the company.
VI	The corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and the shareholders.




OECD Procedures of CG

The Company	
Directors	<p>Every public company should be headed by an effective Board, which should direct, lead and control the Company.</p> <p>There are two key tasks at the top of every public company – conducting the business of the Board, and facilitating executive responsibility for management of the Company's business. There should be a clear division of responsibilities at the head of the Company, which will ensure a balance of power and authority, such that no one individual has unfettered powers of decision.</p>




OECD Procedures of CG

	<p>The Chairman's role in preserving good Corporate Governance is crucial. As the person responsible for running the board, the Chairman should preserve order and facilitate the effective discharge of Board functions.</p> <p>The Board should ensure the availability within it of those with sufficient financial acumen and knowledge to offer guidance on matters of finance.</p> <p>It is preferable for the Board to have a balance of Executive and Non-Executive Directors such that no individual or small group of individuals can dominate the Board's decision taking.</p> <p>The Board should be provided with timely information in a form and of a quality appropriate to enable it to discharge its duties.</p> <p>There should be a formal and transparent procedure for the appointment of new Directors to the Board.</p> <p>All Directors should be required to submit themselves for re-election at regular intervals and at least once in every three years.</p> <p>Boards should periodically appraise their own performance in order to ensure that Board responsibilities are satisfactorily discharged.</p> <p>Shareholders should be kept advised of relevant details in respect of Directors.</p> <p>The Board should be required, at least annually, to assess the performance of the CEO.</p>
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OECD Procedures of CG

Directors' Remuneration	<p>Companies should establish a formal and transparent procedure for developing policy on executive remuneration packages of individual Directors. No Director should be involved in deciding his/her own remuneration.</p> <p>Levels of remuneration of both Executive and Non-Executive Directors should be sufficient to attract and retain the Directors needed to run the Company successfully. A proportion of Executive Directors' remuneration should be structured to link rewards to corporate and individual performance.</p> <p>The Company's Annual Report should contain a Statement of Remuneration Policy and details of remuneration of the Board as a whole.</p>
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OECD Procedures of CG

Relations with Shareholders	Boards should use the AGM to communicate with shareholders and should encourage their participation.
	The Board should implement effective communication with shareholders.
	Further to complying with the requirements under the Companies Act, Securities and Exchange Commission law and Colombo Stock Exchange regulations, as applicable, Directors should disclose to shareholders all proposed material transactions which, if entered into, would materially alter/vary the Company's net asset base or, in the case of a Company with subsidiaries, the consolidated net asset base.



Non Executive Directors (NEDs)


1. **Definition?**
 - are directors who do not have day-to-day operational responsibility for the company. They are not employees of the company or affiliated with it in any other way.
2. **Why we need NEDs?**
 - To have a balance/unbiased view
 - To make "objective judgements"
3. **How many NEDs?**
 - Higher of 2 or 1/3rd of total Board Members
4. **What are other main requirements?**
 - Board to assess annually the independence of NEDs
 - NEDs should have appropriate qualifications, skills and experience and be committed and independent
 - Performance of NEDs should be done annually and should be available for reelection at regular intervals not exceeding 3 years



CG Requirements for Listed Companies in SL:

1. What is the main requirement?
 - Comply with CG requirements as part of the “listing rules”
 - Follow guidelines of Best Practice Code of 2013
2. What are the requirements as part of listing rules?
 - Comply with listing rules applicable for CG
 - State in the annual report that they in compliance with the rules or the reasons for non compliance
3. What are listing rules applicable for CG?

Category	Requirement
NEDs	No of NEDs to be 2 or 1/3 rd of Board whichever is higher where the calculation to be based on Board composition existed at the recent AGM. Any change of the ratio to be rectified within 90 days.
Independent NEDs (INEDs)	If 2 NEDs-Both of them should be INEDs. If more than 2 NEDs, higher of 2 or 1/3 rd of NEDs. All INEDs to submit declaration of independence annually.



CG Requirements for Listed Companies in SL:

Category	Requirement
Disclosures relating to directors	<ul style="list-style-type: none"> • Board to assess the independence of NEDs annually and make disclosures in the annual report on the independence. • If any independence criteria is not met, should disclose those. • Brief resume of all directors should be disclosed in the annual report and for new appointment, resume should be submitted just after the appointment
Remuneration Committee (RC)	<ul style="list-style-type: none"> • RC to be established with all INEDs • When parent and subsidiary are listed, RC of parent company can act as RC for subsidiary. • Board to appoint one INED to be chairman of the RC • RC to recommend remuneration packages of executive directors, CEO and similar positions. Board to take the final decisions • Disclosure to be made in the annual report on the names of members of RC, remuneration policy, aggregate remuneration (excluding EPF, ETF including non cash <u>benefits</u>) paid to all directors
Audit Committee (AC)	<ul style="list-style-type: none"> • RC to be established with all INEDs • When the parent and subsidiary are listed, RC of parent company can act as RC for subsidiary. • Board to appoint one INED to be chairman of the RC • Unless otherwise determined by AC, CEO and CFO should attend AC meetings • Disclosure to be made in the annual report on the names of members of AC and report on <u>the</u> functions



Audit Committee

Audit Committee:

The Board should establish formal and transparent arrangements for considering how they should select and apply accounting policies, financial reporting and internal control principles and maintaining an appropriate relationship with the Company's Auditors

Functions of AC


- Overseeing of the preparation, presentation and adequacy of disclosures in the financial statements of a Listed Entity, in accordance with Sri Lanka Accounting Standards.
- Overseeing of the Entity's compliance with financial reporting requirements, information requirements of the Companies Act and other relevant financial reporting related regulations and requirements.
- Overseeing the processes to ensure that the Entity's internal controls and risk management are adequate to meet the requirements of the Sri Lanka Auditing Standards.
- Assessment of the independence and performance of the Entity's external auditors.
- To make recommendations to the board pertaining to appointment, re-appointment and removal of external auditors and to approve the remuneration and terms of engagement of the external auditors.

Advantages of AC

- Improve quality of financial reporting and public confidence on the objectivity and credibility of F/S
- Create climate of discipline to reduce the risk of fraud
- Enable INEDs to contribute positively and objectively judge
- Providing flat form get things done by CFO/FD which are otherwise difficult
- Provide external auditor a channel for communication for his issues and resolving dispute with managers
- Safeguard internal auditor's independence

Disadvantages of AC

- The executive directors may **not understand** the purpose of an audit committee and may perceive that it detracts from their authority.
- There may be **difficulty selecting** sufficient non-executive directors with the necessary competence in auditing matters for the committee to be really effective.
- The establishment of such a **formalised reporting procedure** may **dissuade** the **auditors** from raising matters of judgement and limit them to reporting only on matters of fact.
- **Costs may be increased.**



Criteria under NEDs will be considered not Independent:

- (a) Has been **employed** by the **listed entity** during the period of two years immediately preceding appointment as director;
- (b) Currently has (or had during the period of two years immediately preceding appointment as a director) a **material business relationship** with the listed entity, whether directly or indirectly;
- (c) Has a **close family member** who is a director, Chief Executive Officer (and/or an equivalent position) in the listed entity;
- (d) Has a **significant shareholding** in the listed entity;
- (e) Has served on the board of the listed entity continuously for a period **exceeding nine years** from the date of the first appointment; provided however, if such director is re-appointed after a period of two years from the date of completion of the preceding nine-year period, he will be considered as 'independent' for the purposes of this Section.

