THE BSE CODE OF BEST PRACTICE (1)

ON CORPORATE GOVERNANCE

SECTION 1: THE COMPANY

A. DIRECTORS

A.1 THE BOARD

Principle A.1 Every company listed on the Domestic Board should be headed by an effective board, which should lead and control the company.

A.1.1 The Board should meet regularly and board meetings should be held at least once in every quarter of a financial year.

A.1.2 The Board should have a formal schedule of matters specifically reserved to it for decision including inter-alia:

• Review/Formulate and monitor implementation of a sound business strategy.
• Ensure that the CEO and Management Team are competent and adopt an effective CEO and Senior Management succession strategy.
• Secure effective information, control and audit systems
• Ensure compliance with legal/ethical standards
• Ensure prevention and management of risks and
• Fulfill such other board functions as are vital, given the scale, nature and complexity of the business concerned.

A.1.3 There should be a procedure agreed by the board for directors in the furtherance of their duties to take independent professional advice if necessary at the company’s expense.

A.1.4 All directors should have access to the advice and services of the board secretary, who is responsible to the board for ensuring that board procedures are followed and that applicable rules and regulations are complied with. Any question of the removal of the board secretary should be a matter for the board as a whole.

A.1.5 All directors should bring an independent judgment to bear on issues of strategy, performance, resources (including key appointments) and standards of conduct.

A.1.6 Every director should dedicate adequate time and effort to matters of the Board and the Company, in order to ensure that the duties and responsibilities owed by him/her to the company are satisfactorily discharged.

A.1.7 Every director should receive appropriate induction on the first occasion that he or she is appointed to the board of a listed company and subsequently as necessary. Training curricula should encompass both general aspects of Directorship as well as

1 Note 1, The BSE acknowledges that The Code of Best Practice on Corporate Governance of the Institute of Chartered Accountants of Sri Lanka and the Executive Summary of the King Report 2002 was relied on when preparing this Code.
matters specific to the particular industry/company concerned.

A.2  CHAIRMAN AND CEO

Principles A.2 There are two key tasks at the top of every company listed on the Domestic Board – the running of the board and the executive responsibility for the running 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.

A.2.1 The posts of Chairman and Chief Executive Officer should not vest in one person. The chairman and chief executive officer should be identified in the Annual Report.

A.2.2 The chairman of the board should preferably be an independent non-executive director.

A.3  CHAIRMAN’S ROLE

Principle A.3 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.

A.3.1 The Chairman should conduct ‘Board proceedings in a proper manner and ensure, inter-alia, that:

- the effective participation of both executive and non-executive directors is secured.
- all directors are encouraged to make an effective contribution, within their respective capabilities, for the benefit of the company.
- balance of power in the board is maintained
- the sense or decision of directors on issues, under consideration, is ascertained
- the board is in complete control of the company’s affairs and alert to its obligations to all shareholders and other stakeholders.

A.4.  BOARD BALANCE

Principle A.4. It is preferable for the board to have a balance of executive and non-executive directors (including independent non-executives) such that no individual or small group of individuals can dominate the board’s decision taking.

A.4.1 For a director to be deemed “Independent” the Board must affirmatively determine that the director has no material relationship with the listed company (directly or as a partner, shareholder, or officer of an organization that has a relationship with the company).

A.4.2 The board should include non-executive directors of sufficient calibre and number for their views to carry significant weight in the board’s decisions. Non-executive directors should comprise not less than one third of the board.
A.4.3 The majority of non-executive directors should be independent of management and free from any business or other relationship, which could materially interfere with the exercise of their independent judgment. Non-executive directors considered by the board to be ‘independent’ in this sense should be identified in the annual report.

**Executive Director** is an individual that is involved in the day to day management and/or is in full time employment of the company and/or its subsidiaries.

**Non Executive Director** is an individual not involved in the day to day management and not a full time salaried employee of the company or its subsidiaries. An individual in the full time employment of a holding company or its subsidiaries, other than the company concerned would also be considered non executive director unless such individual, by his or her conduct or executive authority could be construed to be directing the day to day management of the company and its subsidiaries.

**Independent director** is a non executive director who:

- is not a representative of a shareholder who has the ability to significantly influence management
- has not been employed by the company or its subsidiaries in any executive capacity for the preceding 3 financial years
- is not a member of the immediate family of an individual who is or has been in the past 3 years, employed by the company or the group in an executive position
- is not a professional advisor to the company or its group, other than in his capacity as director
- is not a significant customer or supplier of the company and its group
- has no significant contractual relationship with the company and its group
- is free from any business or other relationship with the company or its group
- is free from any other business or other relationship which could be seen to materially interfere with the individual’s capacity to act in an independent manner.

A.5 **APPOINTMENTS TO THE BOARD**

There should be a formal and transparent procedure for the appointment of new directors to the board.

A.5.1 A nomination committee should be established to make recommendations to the board on all new board appointments. A majority of the members of this committee should be non-executive directors and the chairman should be non-executive director. The chairman and members of the nomination committee should be identified in the annual report.

A.5.2 The nomination committee or in the absence of a nomination committee, the board as whole should annually assess board-composition to ascertain whether the combined knowledge and experience of the board matches the strategic demands facing the company. The findings of such assessment should be taken into account when new Board appointments are considered and when incumbent directors come up for re-election.

A.5.3 Upon the appointment of a new director to the Board, the Company should forthwith disclose to shareholders:

- A brief resume of such director
- The nature of his/her expertise in relevant functional areas
• The names and registered addresses of
directorships or memberships in board-
committees

A.6 APPRAISAL OF BOARD PERFORMANCE

Principle A.6 Boards should periodically appraise their own
performance in order to ensure that prime board
responsibilities are satisfactorily discharged.

A.6.1 The Board should annually appraise itself in the key
responsibilities, inter-alia, of:-

• Reviewing/Formulating and Monitoring
  Implementation of a sound business strategy.
• Ensuring that the CEO and Management Team are
cOMPETENT and the adoption of an effective CEO
and Senior management succession strategy
• Securing effective information, control and audit
  systems
• Ensuring compliance with legal/ethical standards
• Ensuring prevention and Management of risks and
• Fulfiling such other board functions as are vital,
given the scale, nature and complexity of the
business concerned.

Schedule A contains a sample ‘board self-assessment
checklist’ that may be utilized for this purpose.

A.7 APPRAISAL OF CHIEF EXECUTIVE OFFICER

Principle A.7 The Board should be required, at least on an annual
basis to assess the performance of the Chief Executive
Officer.

A.7.1 At the commencement of every fiscal year, the board,
in consultation with the chief executive officer, should
set reasonable financial and non financial targets, in
line with the short, medium and long term objectives
of the company, that are to be met by the chief
executive officer during the course of the year.

A.7.2 The performance of the chief executive officer should
be evaluated by the board at the end of each fiscal
year in order to ascertain whether the targets set by the
board have been achieved and if not, whether the
failure to meet such targets was reasonable in the
circumstances.

B. DIRECTORS’S REMUNERATION

REMUNERATION PROCEDURE

Principle B.1 Companies should establish a formal and transparent
procedure for developing policy on executive remuneration and for fixing the remuneration
packages of individual directors. No director should
be involved in deciding his or her own remuneration.

B.1.1 To avoid potential conflicts of interest, boards of
directors should set up remuneration committees of
independent non-executive directors to make
recommendations to the board, within agreed terms of
reference, on the company’s framework of executive
remuneration and its cost; and to determine on their
behalf specific remuneration packages for each of the
executive directors, including pension rights and any
compensation payments.

B.1.2 Remuneration committees should consist exclusively
of non-executive directors who are independent of
management and free from any business or other relationship which could materially interfere with the exercise of their independent judgment.

B.1.3 The members of the remuneration committee should be listed each year in the board’s remuneration report to shareholders.

B.1.4 The board as a whole, or where required by the Articles of Association, the shareholders should determine the remuneration of the non-executive directors, including members of the remuneration committee, within the limits set in the Articles of Association. Where permitted by the Articles, the board may however delegate this responsibility to a small sub-committee, which might include the chief executive officer.

B.1.5 Remuneration committees should consult the chairman and/or chief executive officer about their proposals relating to the remuneration of other executive directors and have access to professional advice inside and outside the company.

SHARE OPTIONS/DIRECTORS TRANSACTIONS

Principle B.2 Notwithstanding Listing Rule 10.7 (d) no discounts should be offered to employees on share options.

B.2.1 Executive share options should not be offered at a discount (i.e. less than prevailing market price at the time the share option price is determined)

B.3 DISCLOSURE OF REMUNERATION

Principle B.3 The Company’s annual report should contain a statement of remuneration policy and details of remuneration of the board as a whole.

B.3.1 Total of the executive directors and the total of the non executive directors remuneration and not the individual remuneration to be disclosed.

B.3.2 Remuneration should include bonus payment and share option schemes. For this purpose the value of share options should be the difference between the market price and the exercise price on the day such option is exercised.

C. RELATIONS WITH SHAREHOLDERS

CONSTRUCTIVE USE OF THE AGM

Principle C.1 Boards should use the AGM to communicate with investors and encourage their participation.

C.1.1 Companies should propose a separate resolution at the AGM on each substantially separate issue and should in particular propose a resolution at the AGM relating to the adoption of the report and accounts.

C.1.2 Companies should consider conducting meetings on the basis of a poll in relation to special business, or where contentious issues are under consideration, in order to ensure that all votes of shareholders (whether in person, by proxy or representation) at company meetings are taken into account. The results of all decisions taken at the company meetings should be
publicly disseminated, in the most appropriate form, immediately on conclusion of the meeting to ensure that all shareholders (particularly those who were not in attendance or were unable to attend) are promptly informed or at least have ready access to that information.

C.1.3. The chairman of the board should arrange for the chairmen of the audit, remuneration and nomination committees to be available to answer questions at the AGM if so requested by the chairman.

C.1.4. Companies should circulate with every Notice of General Meeting, a summary of the procedures, governing voting at General Meetings.

C.2. “MAJOR’ TRANSACTIONS

Principle C.2 In terms of a circular issued in terms of Listing Rule 9.31 directors should also disclose to shareholders all proposed corporate 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 group net asset base.

D. ACCOUNTABILITY AND AUDIT

D.1 FINANCIAL REPORTING

Principle D.1 The board should present a balanced and understandable assessment of the company’s position and prospects.

D.1.1 The Board’s responsibility to present a balanced and understandable assessment extends to interim and other price-sensitive public reports and reports to regulators as well as to information required to be presented by statutory requirements.

D.1.2 The Directors Report, which forms part of the Annual Report, should contain declarations by the directors to the effect that:

- The company has not engaged in any activities, which contravene laws and regulations.
- The directors have declared all material interests in contracts involving the company and refrained from voting on matters in which they were materially interested.
- The company has made all endeavours to ensure the equitable treatment of shareholders.
- The business is a going concern, with supporting assumption or qualification as necessary.
- They have conducted a review of the internal controls which should cover financial, operational and compliance controls and risk management.

D.1.3 The Annual report should contain a statement setting out the responsibilities of the board for the preparation of financial statements, together with a statement by the auditors about their reporting responsibilities.

D.1.4 The Annual Report should contain a Management Report, discussing, among other issues:

- Industry structure and development
- Opportunities and threats
• Risks and concerns
• Internal Control Systems and their adequacy
• Financial performance
• Material developments in Human Resources/Industrial relations
• Prospects for the future

D.1.5. In the event that the net assets of the company falls below one third of the company’s shareholders funds, the directors shall forthwith summon an Extraordinary General Meeting of the company to notify shareholders of the position and of remedial action being taken.

D.2 **INTERNAL CONTROL**

**Principle D.2** The board should maintain a sound system of internal control to safeguard shareholders’ investment and the company’s assets.

D.2.1 The directors should, at least annually, conduct a review of the effectiveness of the group’s system of internal controls and should report to shareholders that they have done so. The review should cover all controls, including financial, operational and compliance controls and risk management.

D.2.2 Companies, which do not have an internal audit function, should from time to time review the need for one.

D.3 **AUDIT COMMITTEE AND AUDITORS**

**Principle D.3** The board should establish formal and transparent arrangements for considering how they should apply the financial, reporting and internal control principles and for maintaining an appropriate relationship with the company’s auditors.

D.3.1 The board should establish an audit committee of at least three directors, all non-executive, with written terms of reference which deal clearly with its authority and duties. The members of the committee, a majority of whom should be independent non-executive directors, should be named in the report and accounts.

D.3.2 The duties of the audit committee should include keeping under review the scope and results of the audit and its effectiveness and the independence and objectivity of the auditors.

D.3.3. **The audit committee should draw up a recommendation to the board for consideration and acceptance by the shareholders for the appointment of the external auditors.**

D.3.4. The audit committee should ensure that the independence of auditors are maintained and that any consultancy or any work contracted with the auditing firm will not have a material impact on the auditor’s independence.

D.3.5. The audit committee should set principles for recommending to the board rotation and remuneration of auditors.

D.4 **CORPORATE GOVERNANCE**
Principle D.4 Directors should disclose in the Company’s Annual Report the extent to which the company has adhered to the Code of Best Practice on Corporate Governance, and where there has been no compliance with the Code, to give reasons.

SCHEDULE A
BOARD COLLECTIVE ASSESSMENT CHECK LIST

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<thead>
<tr>
<th>Key Function</th>
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<th>B</th>
<th>D</th>
<th>C</th>
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<tbody>
<tr>
<td>1. Understanding of the strategy setting process within the company</td>
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<td>2. Seeking and contributing views and opinions on strategic options available to the company and in strategic decision making.</td>
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<td>3. Understanding the strategic choices before the company and the basis on which particular choices have been made.</td>
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<td>4. Mechanism to monitor the progress in implementing strategic decisions</td>
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<td>5. Information on / knowledge about budgetary targets and other</td>
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6. Knowledge and degree of satisfaction regarding the integrity of the company’s accounting and financial reporting systems including the independence and adequacy of coverage.

7. Information on / understanding of the risks associated with the controls and systems that are in place to manage such risk.

8. Information / knowledge on the effectiveness of systems and controls referred to in 6 and 7 above.

9. Information on and the level of confidence regarding compliance by the company with legal, ethical and regulatory requirements.

10. Knowledge and level of satisfaction of the shareholders, the general public and other stakeholders on corporate performance and financial reporting.
11. A formal process for evaluating the performance of the CEO and his top team.

12. Understanding the compensation philosophy “to retain and motivate staff in a manner appropriate for the business”.

13. Understanding the succession plan to ensure comprehensive staff succession – “to ensure talent availability and address expectations of high potential and high quality staff.

14. Leveraging the skills, expertise and contacts of individual board members in the furtherance of the company’s business.

15. Monitoring and managing conflicts of interest of management, board members and shareholders including misuse of corporate assets and abuse in related party transactions.

16. Adequacy of the knowledge base, commitment, and level of participation relation to individual board members and collectively as a board.

17. Equitable distribution of responsibilities among the directors.

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<tr>
<th>Key Function</th>
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<tr>
<td>Adequacy of compensation in relation to time, demands and responsibilities</td>
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<td>18. A formal and transparent board nomination process.</td>
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