



**REPUBLIC OF ALBANIA  
MINISTRY OF ECONOMY, TRADE AND ENERGY  
COMPETITIVENESS POLICY DEPARTMENT**



# CORPORATE GOVERNANCE CODE

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for Unlisted Joint-Stock Companies  
in Albania

Drafted with the Assistance of International Finance Cooperation (IFC)

**IMPORTANT:**

**This document is based on relevant international best practices.**

**The Corporate Governance Code complies with relevant company and other legislation in force and regulation in effect in the Country.**

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# **Corporate Governance Code for Unlisted Joint-Stock Companies in Albania**

*Based on the Corporate Governance Guidance  
and Principles for Unlisted Companies in  
Europe, an initiative of ecoDa<sup>1</sup>.*

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<sup>1</sup> ecoDa, the European Confederation of Directors' Associations, is a not-for-profit association acting as the "European voice of directors", active since March 2005 and based in Brussels. For further information on ecoDa, visit: [www.ecoda.org](http://www.ecoda.org)



## **INTRODUCTION**

The most widely used definition of corporate governance is the one used by OECD, in its Principles of Corporate Governance, where corporate governance is defined as involving a set of relationships between a company's management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined. Good corporate governance practices should provide proper incentives for the board and management to pursue objectives that are in the interests of the company and its shareholders and should facilitate effective monitoring.<sup>2</sup>

This Corporate Governance Code for Unlisted Joint-Stock Companies in Albania (“the Code”) focuses on specificities of corporate governance for unlisted companies. The corporate governance of listed companies, which in principle have large number of external minority shareholders and may be run by professional managers, without significant ownership stake, tends to focus on ensuring that external shareholders can exercise effective oversight and control over management and the board. In contrast, most unlisted companies are owned and controlled by single individual or coalition of company insiders (e.g. a family). Good governance of unlisted companies, in this context, is not a question of protecting the interests of absentee shareholders. Rather, it is concerned with establishment of a framework of company processes and attitudes that add value to the business and help ensure long-term continuity and success.<sup>3</sup>

This Code is only a best practice reference for unlisted companies in Albania, aimed at designing a framework of best practices being over and above the minimum legal requirements. Thus it is not a regulation that companies would be obliged to comply with. Also, it is not soft-law document in relation to which companies will have to report if they comply with or to explain why they do not comply with it (“comply-or-explain” principle). Rather, it is an overview of the best practices in relation to governance of unlisted companies in the moment of its preparation, and it is intended to serve as reference and inspiration for Albanian companies to develop sound governance framework.

In any case, for avoidance of doubt, this Code should be read in conjunction with relevant national legal and regulatory acts, and when different interpretations might arise, the ones as per the relevant national and regulatory acts would prevail.

In principle, this Code is cross referenced with the relevant laws, where appropriate, primarily with Law on Entrepreneurs and Companies, but also with other relevant laws. Please note, however, that in some instances, naturally, not the same wording from the relevant cross-references laws has been used.

The Code has the following structure:

- It comprises 14 principles, 9 of which are relevant for all unlisted joint-stock companies in Albania, and 5 of which are relevant only for large and/or more complex unlisted joint-stock companies in Albania.
- In the First Part of the Code a list of these 14 principles is provided.

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<sup>2</sup> OECD Principles of Corporate Governance, 2<sup>nd</sup> Edition, 2004, p.11

<sup>3</sup> See further in ecoDa Corporate Governance Guidance and Principles for Unlisted Companies in Europe, p. 12

- **In the Second Part of the Code these 14 principles are further elaborated. Under each of the principles, Key Points and, where appropriate, further Notes elaborating the Principle are provided.**

**Please note that in Albania joint-stock companies are free to choose between one-tier system of governance, with Board of Directors comprising both executive and non-managing directors, and two-tier system of governance, with Supervisory Board and Managing Directors. For purposes of clarity, and in line with relevant international theory and best practices, this Code uses the generic term “board” to mean: Board of Directors (in companies with one-tier system of governance) and both Supervisory Board and Managing Directors (in companies with two-tier system of governance). In this respect, the case-by-case interpretations in relation to this should be based on the legal provisions and concrete practices in individual companies.**

**The Corporate Governance Code for unlisted companies in Albania is drafted with by the international experts of International Finance Corporation (IFC). A special contribution especially with regard to its alignment with Law on Entrepreneurs and Commercial Companies have been given by the GIZ experts.**

## FIRST PART

### **Corporate Governance Principles for All Unlisted Joint-Stock Companies**

*Principle 1: Shareholders of companies should establish an appropriate constitutional and governance framework for the company.*

*Principle 2: Every company should strive to establish effective board which is collectively responsible for the long-term success of the company, including the definition of the corporate strategy.*

*Principle 3: The size and composition of the board should reflect the scale and complexity of the company.*

*Principle 4: The board should meet sufficiently regularly to discharge its duties, and should be supplied in a timely manner with appropriate information.*

*Principle 5: Levels of remuneration should be sufficient to attract, retain and motivate executive and non-managing directors of the quality required for running the company successfully. Individuals should not be responsible for setting their own remuneration. Arrangements for remunerating directors should be approved by shareholders, especially when this involves grants of shares and options.*

*Principle 6: The board is responsible for risk oversight and should maintain a sound system of internal control to safeguard company's interests and shareholders' investments.*

*Principle 7: There should be a dialogue between the board and the shareholders based on the mutual understanding of objectives. The board as a whole has responsibility for ensuring that a satisfactory dialogue with all shareholders takes place.*

*Principle 8: All directors should receive induction on joining the board and should regularly update and refresh their skills and knowledge.*

*Principle 9: Family-controlled companies should establish family governance mechanisms that promote coordination and mutual understanding amongst family members, as well as organize the relationship between family business governance and corporate governance.*

## **Corporate Governance Principles Applicable to Large and/or More Complex Unlisted Joint-Stock Companies**

*Principle 10: There should be a clear division of responsibilities at the head of the company between the running of the board and the running of company business. No one individual should have unfettered powers of decision.*

*Principle 11: The board should contain directors with sufficient mix of competences and experience. No single person (or small group of individuals) should dominate the board's decision making. Due regard should be paid for the benefits of diversity on the Board, including gender.*

*Principle 12: The board should establish appropriate board committees in order to allow a more effective discharge of its duties.*

*Principle 13: The board should undertake periodic appraisal of its own performance and that of each individual director.*

*Principle 14: The board should present a balanced and understandable assessment of the company's position and prospects for stakeholders, and establish a suitable program of stakeholder engagement.*



## SECOND PART

### Corporate Governance Principles for All Unlisted Companies

**Principle 1:** Shareholders of companies should establish an appropriate constitutional and governance framework for the company.

**Key points:**

- *Shareholders should establish a basic framework of corporate governance* through the company's constitutional documents (e.g. statute or bylaws).
- *The powers and role of the board should be clearly defined*, including establishment of those issues which remain up to the shareholders to decide and those responsibilities which the board retains for itself rather than delegating to management (see also Principle 2).
- *In the same time, shareholders should minimize the extent to which the basic framework of corporate governance constrains the ability of the board to shape the detailed governance framework.*
- *Due care should be taken that in the development of the governance framework of the company all stakeholders are properly consulted*, most notably the employees. The constitutional framework should, where appropriate, take into consideration the corporate social responsibility of the company.

**Principle 2:** Every company should strive to establish effective board which is collectively responsible for the long-term success of the company, including the definition of the corporate strategy.

**Key points:**

- *The responsibilities of the board include setting company's strategy, providing leadership to put it into effect, supervising the management of the business, and reporting to shareholders on the stewardship of the company.*
- *All members of the board are bound by the company's best interest.*
- *All directors must undertake decisions in the best interest of the company.* As the company develops, appointing independent directors onto the board can help in focusing the board on the corporate interest.
- *The board should elect a chairman.* The chairman is responsible for leadership of the board, ensuring its effectiveness on all aspects of its role and setting its agenda.
- *The board should set the company's strategic objectives*, and ensure that the necessary financial and human resources are in place for the company to meet its objectives.
- *The board is responsible for monitoring and evaluating management performance.*
- *The board should set the company's values and standards* and ensure that its obligations to shareholders and other stakeholders are understood and met.
- *The board should be involved in the strategic development process* and – as a minimum – approve the strategy, and ensure that it lies within the shareholders' interests.
- *It is the responsibility of the board to ensure that the company complies* with its charter as well as relevant legal, regulatory and governance requirements.
- *There should be a formal schedule of matters which states which matter are specifically reserved for the board's decision* and which are to be delegated to management.

- ***Where directors have concerns which cannot be resolved*** about the running of the company or a proposed action, they should ensure that their concerns are recorded in the board minutes.
- ***Comprehensive observance of confidentiality*** is of paramount importance for undertaking of quality open discussion on the board meetings, which in turn is a pillar of good corporate governance.

#### Notes to Principle 2:

- *Joint-Stock Companies in Albania are entitled to choose between one-tier system of governance (with Board of Directors, having both oversight and management function, and comprising both administrators and non-managing directors), and two-tier system (with Supervisory Board, having the oversight function, comprising non-managing directors; and Managing Directors, having the management function, comprising administrators).*
- *In this Corporate Governance Code for Unlisted Companies in Albania (“the Code”) when reference is made to the “board” it refers to the company’s board in its entirety, i.e. it refers to Board of Directors in one-tier system of governance and to both Supervisory Board and Managing Directors in the case of two-tier system of governance.*
- *In the case where a company chooses a one-tier system, the Board of Directors provides directives to the Managing Directors and monitors and supervises that these are implemented; ensures that the company fulfills its compliance obligations; prepares relevant annual reports; hires and determines remuneration of the Managing directors and takes overall care for appropriate navigation of company’s business.*
- *In the case where a company chooses a two-tier system, Managing Directors lead the company and decide on the manner of implementation of the business policy while the Supervisory Board assesses the policy implementation and controls company’s compliance.*
  - *In line with best practices the cooperation between Managing Directors and Supervisory Board should be along the following lines:*
    - *Managing Directors and Supervisory Board should cooperate closely to the benefit of the company.*
    - *Managing Directors and Supervisory Board should have joint responsibilities to provide sufficient information to the Supervisory Board*
    - *Managing Directors and Supervisory Board should engage in open discussion, with comprehensive observance of confidentiality.*
- *All members of the board are bound by the company’s best interest. This includes, but is not limited to the following:*
  - *To perform their duties in good faith, including with respect to ensuring environmental sustainability of the company’s operations.*
  - *To exercise the powers only for the purposes for which these powers have been established.*
  - *To give adequate consideration to matters to be decided.*
  - *To avoid actual and potential conflicts between personal interests and those of the company.*
  - *To exercise reasonable care and skill in the performance of their function.*
- *A schedule of matters reserved for the general meeting of shareholders would typically include the following*

- Definition of corporate commercial policy
  - Approval of the annual accounts, financial statements and progress reports of business development
  - Distribution of annual profits.
  - Approval of changes to the charter/by-laws and/or changes to capital structure
  - Appointment, remuneration and dismissal of directors, members of the supervisory board, liquidators and certified auditors
  - Changes in the rights attached to particular types and classes of shares,
  - Re-organization, transformation and dissolution of the company
- *A schedule of matters potentially reserved for the board* would typically include:
- Definition of corporate goals, strategy and structure
  - Responding to shareholders and third parties
  - Supervising and controlling company progress
  - Supervising the Administrator (or Chief Executive Officer (CEO))
  - Approval of corporate plans
  - Approval of operating and capital budget
  - Approval of major corporate actions (e.g. acquisitions, disposals, commencing or terminating of business activities)
  - Approval of financial statements
  - Approval of borrowings or creditor guarantees (possible above certain amount)
  - Policy on external communications, e.g. with regulators, shareholders and/or the media
  - Definition of authorities delegated to management
  - Nominating and (recommendation for) dismissal of the Administrator (CEO), and/or on his/her remuneration (possibly also of other top management, in consultation with the Administrator (CEO))
- *The board should maintain a compliance schedule* which shows when various financial, legal, and regulatory requirements must be completed, and who is responsible for each item. Such schedule is likely to include:
- Obligations relating to the preparation and filing of financial statements
  - Tax compliance
  - Banking facilities and covenants
  - Health and safety compliance
  - Insurance
- *A schedule of powers delegated to management* is likely to cover the following issues:
- Preparing strategic proposals, corporate plans, and budgets
  - Executing the strategy agreed upon by the board
  - Executing actions in relation to board decisions on investments, mergers, and acquisitions, etc.
  - Opening bank accounts and authorizing financial payments
  - Signing of contracts
  - Signing of internal company regulatory documents
  - Powers of attorney
  - External communication
  - Staff recruitment and remuneration
  - Establishing a system of internal control and risk management
  - Health and safety operations

- *The board should promote high standards of professional and business conduct, which should be summarized in a Code of Business Conduct, which should state the company's expectations in relation to:*
  - o Compliance with laws and regulations
  - o Standards of customer services
  - o Conflicts of interest
  - o Gifts or preferential treatment in respect of suppliers, customers etc.
  - o The need for integrity and ethical business practice
  - o Company obligations to the general well-being of the company
  - o Support for employee personnel development.

With regards to conflict of interests, the board members and company's key personnel must inform the board and shareholders directly if they, directly or on behalf of third parties, have a material interest in transactions directly involving the company. They also have to inform about any change in ownership (particularly if this allows a significant or even controlling influence)

In reference to the conflict of interest, directors should always declare potential conflicts of interest to the rest of the board and be prepared to leave the board entirely in cases where such conflicts may trigger the success of the company. Penalties should apply in case of non-compliance of the director with such a rule.

**Principle 3: The size and composition of the board should reflect the scale and complexity of the company.**

**Key points:**

- *The board should be at least 3 or a higher uneven number of members, but of not more than 21 and in any case not as large as to be unwieldy.* The balance of skills and expertise should be appropriate for the requirements of the business. Changes to the board's composition should be manageable without undue disruption. Directors are natural persons, the majority of whom shall be independent and non-managing.
- *There should be an explicit procedure for the appointment of new directors to the board.* Appointments to the board should be made after careful examination against objective criteria, including gender.
- *The board should satisfy itself that plans are in place for orderly succession for appointments to the board and senior management.* The aim is to maintain an appropriate balance of skills and experience within the company and on the board.
- *The period of appointment of directors should be carefully considered.* Board appointments should be for up to three years, with the possibility of re-election, and subject to periodic renewal so as to ensure planned and progressive refreshing of the board.

**Principle 4: The board should meet sufficiently regularly to discharge its duties, and should be supplied in a timely manner with appropriate information.**

**Key points:**

- *Board meetings should be organized in such a way as to maximize the contribution of directors,* encouraging each director to take active part in an informed decision making process.
- *The chairman is responsible for ensuring that the directors receive accurate, timely, and clear information.*

- **Administrators have obligation to provide such information.** However, directors should seek clarification or amplification from administrators where necessary. The board should establish explicit procedures which allow directors to approach management for further information.
- **The board should ensure that all directors – especially non-managing directors – have access to independent professional advice** at company’s expense where they judge it necessary to discharge their responsibilities as directors.

Notes to Principle 4:

- *The typical structure for board meetings* is as follows:
  - An agenda should be prepared by the chairman
  - The agenda and supporting papers (if any) should be circulated in advance to the meeting, allowing directors sufficient time to prepare.
  - Written minutes of board meetings should be taken. All decisions should be recorded (including dissenting opinions), along with assigned tasks and timescales. The minutes should also give an overview of the main topics discussed at the meeting.
  - Board meetings should monitor progress against approved plans and budgets, and ensure full coverage of matters reserved for the board.
- *In the event of meetings convened through electronic means* i.e. teleconference, afterwards a minuted and signed proceeding of a teleconference or video conference should constitute proof of the board members participation and such minutes recorded as circular resolutions, should be signed and confirmed by the directors who have attended the meeting through video/tele conferencing.

**Principle 5: Levels of remuneration should be sufficient to attract, retain and motivate executive and non-managing directors of the quality required for running the company successfully. Individuals should not be responsible for setting their own remuneration. Arrangements for remunerating directors should be approved by the shareholders, especially when this involves grants of shares and options.**

Key points:

- **A clear distinction must be made between the remuneration of executive and non-managing directors.** The former are engaged in the company on full-time employee basis, and are responsible for its operational activities. In contrast, non-managing directors are “office holders” rather than company employees, and dedicate their time to the company on a part-time basis. Remuneration structure should reflect these differing roles.
- **Members of the board are accountable to shareholders for their remuneration.** However, in practice, many boards will themselves define and propose to the meeting of shareholders any change in their annual remuneration.
- **Levels of remuneration for non-managing directors should reflect the time commitment and responsibilities of the role.** The total compensation of Management Board members comprises the monetary compensation elements, pension awards, other awards, especially in the event of termination of activity, fringe benefits of all kinds and benefits by third parties which were promised or granted in the financial year with regard to Management Board work. The compensation structure must be oriented toward sustainable growth of the enterprise. The monetary compensation elements shall comprise fixed and variable elements. The Supervisory Board must make sure that the variable compensation elements are in general based on a multiyear assessment. Both positive and negative developments shall be taken into account when

determining variable compensation components. All compensation components must be appropriate, both individually and in total, and in particular must not encourage taking unreasonable risks.

- **Caution should be expressed when linking non-managing directors' remuneration to company's performance**, in order to provide incentives to non-managing directors to remain vigilant in control of management and to de-stimulate excessive risk-taking.
- **The board should develop a formal executive remuneration policy and transparent procedure for implementing policy**, e.g. in terms of fixing the remuneration packages of individual and non-managing directors, specification of the relevant benchmarks and performance criteria in the remuneration process and the level of information disclosure regarding remuneration issues.
- **No one should be involved in deciding on his/her own remuneration.**
- **Boards should compare the remuneration of the company's executive and non-managing directors with that of other relevant companies.** But they should use such comparisons with caution, in view of the risk of upwards ratchet of remuneration levels with no corresponding improvement in performance.
- **Boards should be sensitive to pay and employment conditions elsewhere in the company**, especially when determining annual salary increases.
- **A significant proportion of executive remuneration should be structured so as to link rewards to corporate and individual performance.** They should be designed to align their interests with those of shareholders and other stakeholders, and give these executive directors incentives to perform at highest levels.
- **When applicable, the board should consider the financial implications of early termination of executive directors' terms of office.** In addition, careful thought should be given to notice or contract periods. The aim should be to avoid rewarding poor performance.

#### Notes to Principle 5:

- *Good practices in executive remuneration* is likely to consider the some of the following elements in its design:
  - A balance between fixed and variable pay, and the linkage of variable pay to pre-determined performance criteria
  - Deferral of some proportion of variable pay
  - In cases where share are granted, a minimum vesting period. A requirement to retain some proportion of those shares until the conclusion of employment
  - The reclaim of variable pay paid on the basis of data which subsequently proves to be manifestly misstated (“clawback”)
  - A limit on severance pay, and non-payment of severance pay in case of poor performance

**Principle 6: The board is responsible for risk oversight and should maintain a sound system of internal control to safeguard the company's interests and the shareholders' investment.**

#### **Key points:**

- **The board should attempt to identify the main strategic and operational risks facing the company.** It should satisfy itself that the level of strategic risk is acceptable and that all material risks are being appropriately managed.

- ***The board should establish formal and transparent arrangements for applying financial reporting and internal control policies***, and for maintaining an appropriate relationship with company's auditors.
- ***The board should periodically assess the need to establish or redesign its formal internal controls and risk management function(s)***. Moreover, a periodic check on the effectiveness of the company's approach towards internal control is necessary. Such review should cover all material controls, including financial, operational and compliance controls, and risk management systems.

#### Notes to Principle 6:

- *It is useful for companies to develop a basic risk register*, which is reviewed by the board on regular basis. This register may contain the following categories of information:
  - A description of the main risks facing the company
  - The impact should this event actually occur
  - The probability of its occurrence
  - A summary of the planned response should the event occur
  - A summary of risk mitigation (the actions that can be taken in advance to reduce the probability and/or impact of the event).
- *A company manual* should be available to all employees, and should outline policies and procedures relating to specific risks, to which company is exposed. For example, such policies should be developed with regard to:
  - Anti-corruption
  - Anti money-laundering
  - Cash management
  - Monitoring of banking covenants
  - Business continuity
  - Data security and reliability
  - Records managements
  - Regulatory and standards compliance
  - Health and safety compliance
- *Procedures which are likely to support an effective internal control environment* are likely to include:
  - Authorization limits
  - Segregation of duties
  - Accounting reconciliations and monitoring cash-flow
  - Suitable qualifications and training
  - Budgetary controls
  - Controls over funds, expenditures and access to bank accounts
  - Security of premises and control over assets
- *Internal audit* is an independent and objective assurance that helps the company achieve its objectives by bringing a systematic, and disciplined approach to evaluate and improve effectiveness of risk management, internal controls and governance processes. When defining the internal audit function in the company, the following issues should be taken into consideration:
  - The internal audit function should have full independence.

- While the internal audit function should communicate with management in the performance of its duties, it should be clear that management does not oversee the function.
- The internal audit function should report directly to the board.
- The internal audit function should be able to perform work free of interference and should be able to undertake assignments on its own initiative.
- The internal audit function should not be required to disclose its work-plans or scheduled audits or have its work plan or budget approved by management.
- The internal audit function should have an adequate and independent budget to allow it to perform its roles effectively for the benefit of the company and the shareholders.
- Each internal auditor should have clear Terms of Reference, allowing him/her to examine all areas in which the company operates and in all the company's functions and processes. These Terms of Reference should include authorization of the internal auditor to:
  - review accounting policies and practices, reports and financial reporting policies;
  - determine compliance with relevant laws and regulations and internal company by-laws and codes; and
  - Contribute to the review of the qualifications, independence and capabilities of external auditors.

**Principle 7: There should be a dialogue between the board and the shareholders based on the mutual understanding of objectives. The board as a whole has responsibility for ensuring that a satisfactory dialogue with all shareholders takes place.**

**Key points:**

- *The board should keep in touch with shareholders opinion* whatever ways are most practical and efficient, including through information and communication technology facilities, where appropriate.
- *The chairman has particular responsibility for the effectiveness of communication between shareholders and the board*, and should discuss corporate governance and strategy with shareholders and, where appropriate, other stakeholders, primarily employees.
- *The chairman has primary means of ensuring that the views of the shareholders are communicated to the board as a whole*. However, other directors should also be offered the opportunity of attending meetings with shareholders.
- *A key role of the chairman is to set the agenda of the general meetings of shareholders.*
- *The relationship with the shareholders should be viewed as a continuous process* and not limited to an annual formal meeting.
- *All directors should attend general meetings of shareholders.*

**Principle 8: All directors should receive induction on joining the board and should regularly update and refresh their skills and knowledge.**

**Key points:**

- *The rigor and formality of the induction should reflect the size and complexity of the enterprise.*
- *The chairman should ensure that the directors continually update their skills, and obtain the knowledge and familiarity with the company* required to fulfill the role on the board.



- *The chairman should encourage board members to engage in professional training* that specifically enhances their functioning as company directors.

**Principle 9: Family-controlled companies should establish family governance mechanisms that promote coordination and mutual understanding amongst family members, as well as organize the relationship between family business governance and corporate governance.**

**Key points:**

- *The choice of family business governance process* will depend on the size of the business, the number of family members and the degree of involvement of family members in the business.
- *A family constitution or protocol* should outline the vision and objectives of the family for the business. It should define the roles of family business governance bodies, and their relationships with the board. It should also state the key family policies, e.g. relating to family members' employment, transfer of shares and succession of Administrator (CEO).
- *Family governance bodies* – such as a family assembly and a family council – provide family members with a forum in which to discuss the affairs of the family and the family business, and assist the development of a coordinated family business governance approach.
- *A clear distinction in governance status must be made between family governance institutions and formal governance structures of the company.* The role of the board, the general meeting of shareholders, management, etc. must be fully understood by family members.

**Notes to Principle 9:**

- *A family constitution* outlines how the family business governance should work. It clarifies, among other issues, the family's approach with respect to:
  - The family's values, mission and vision.
  - The role of the family institutions, such as family assembly and the family council.
  - The role of the board, and its relationship with the family institutions.
  - Policies regarding important family issues, such as employment policies with respect to family members, restrictions on transfers of shares, and succession policy with respect to the Administrator (CEO).
  - The nomination of the family members on the board.

## **Corporate Governance Principles Applicable to Large and/or More Complex Unlisted Companies**

**Principle 10:** There should be a clear division of responsibilities at the head of the company between the running of the board and the running of company business. No one individual should have unfettered powers of decision.

### **Key points:**

- *In larger companies with unitary boards, the roles of chairman and Administrator (CEO) should not be exercised by the same individual.* The division of responsibilities between the chairman and the Administrator (CEO) should be clearly established, set out in writing, and agreed by the board.
- *Over time, companies should strive to nominate an independent chairman.* However as an interim measure, appointment of the incumbent Administrator (CEO) (e.g. the founding owner of the company or the *pater familias*) as chairman may be the most viable option.

**Principle 11:** The board should contain directors with sufficient mix of competences and experience. No single person (or small group of individuals) should dominate the board's decision making. Due regard should be paid for the benefits of diversity on the Board, including gender.

### **Key points:**

- *The largest unlisted enterprises and the unlisted enterprises working towards a public listing on a regulated market – should have majority non-managing and independent directors on their boards.*
- *Care should be taken to ensure that non-managing or independent appointees have enough time available to devote to the job.* This is particularly important in the case of chairmanships. The letter of appointment should set out the expected time commitment. Non-managing directors or independent directors should undertake that they will have sufficient time to meet what is expected from them. The other significant commitments should be disclosed to the board before appointment and the board should be informed on subsequent changes.
- *The chairman should facilitate the effective contribution of non-managing and independent directors and ensure constructive relations between all directors.*
- *Non-managing directors and independent directors should constructively challenge and help develop proposals on strategy.*
- *Non-managing and independent directors should scrutinize the performance of management* in meeting agreed goals and objectives and monitor the reporting on performance.
- *Non-managing directors and independent directors should satisfy themselves on the integrity of financial information and make sure the financial controls and systems on risk management, including executive directors.* They should also play a leading role in appointing, and where necessary removing, and in succession planning.
- *The chairman may decide to hold meetings with the non-managing director without the executive directors present,* including executive sessions at which the performance of executive directors would be assessed.
- *Non-managing directors or independent directors may be appointed for a specified term* (e.g. an initial mandate of maximum three years, possibly renewable two times.) Decision to extend the terms of service should balance the need for company-specific experience (which may take time to acquire) and the benefits of progressive refreshing of the board. It should also be

recognized that serving for many years on a board may affect external perceptions of non-managing director's independence.

- ***On resignation, a non-managing director should provide a written statement to the chairman, for circulation to the board, if they have significant concerns about the running of the company.***

Notes to Principles 11:

- *The key benefits of including independent non-managing directors on the board include the following:*
  - Bringing outside perspective on strategy and control
  - Adding new skills and knowledge that may not be available within the firm
  - Bringing objective and independent view from the one of the shareholders
  - Making hiring and promotion decisions independent from family ties (in family owned companies)
  - Bringing independent view whenever there may be conflicts of interest within the board
  - Acting as balancing element between the different shareholders (e.g. members of the family) and, in some cases, serving as objective judges of disagreements amongst significant shareholders or managers
  - Benefiting from their business connections and contacts
  
- *Factors that may be of relevance in establishing the substantive and perceived independence of non-managing directors include:*
  - Has not in recent years been an employee of the company
  - Has not a material business relationship with the company
  - Does not receive (additional) remuneration from the company during the period of appointment as a director (apart from director's fee)
  - Does not have close family ties with any of the company's advisers, directors or senior employees
  - Does not hold cross-directorships or have significant links with other directors through involvement in other companies or bodies
  - Does not represent a significant shareholder
  - Has not served on the board for an extended period
  
- *Independent non-managing directors should be appointed with a formal Letter of Appointment, that should contain the following:*
  - Specification of the expectation of the Board from the appointed director;
  - The Board-level committee(s) in which the director is expected to serve and its tasks;
  - The fiduciary duties that come with such an appointment;
  - The term of the appointment;
  - The Code of Business Conduct that the company expects its directors and employees to follow;
  - The list of actions that a director cannot do in the company;
  - The liabilities that accompany such a fiduciary position, including whether the concerned director is covered by any professional insurance;
  - The remuneration.

Such letter stating the terms and conditions of appointment of any independent director should form a part of the disclosure to shareholders at the time of the ratification of his/her appointment or re-appointment to the Board.

**Principle 12: The board should establish appropriate board committees in order to allow a more effective discharge of its duties.**

**Key points:**

- *A company's committee structure should be proportionate to the needs of the company.* However, most large unlisted enterprises are likely to require a nomination committee, remuneration committee, compliance committee and audit committee. Other committees may be established if required in particular circumstances.
- *The board should define in writing the terms of reference of various committees*, explaining their role and the advisory authority delegated to them by the board. These terms of reference should be reviewed by the board on a periodic basis.
- *Committees should be provided with sufficient resources to undertake their duties.*
- *Independent non-managing directors* should play a significant role in boardroom committees and should constitute a majority on the audit and remuneration committees.

**Notes to Principle 12:**

- *The role of the nomination committee* is to evaluate the balance of skills, knowledge and experience on the board, as well as amongst management, to prepare a description on the roles and capabilities required for particular board appointment and to propose a management succession plan; to search for, to evaluate, to shortlist and to recommend appropriate independent directors subject to the broad directions of the full board; and to evaluate and recommend the appointment of executive directors.
- *The role of the remuneration committee* is to propose the remuneration of all administrators, including pension rights, and defines and monitors the level and structure of remuneration for senior management.
- *The role of the compliance committee* is to ensure that the company is compliant with all relevant internal and external rules and standards.
- *The role of the audit committee* include:
  - To monitor the integrity of the financial statements of the company
  - To review the company's internal controls and risk management systems
  - To monitor and review the effectiveness of the company's internal audit function
  - To make recommendations to the board in relation to the appointment or removal of the external auditor
  - To approve the remuneration and terms of engagement of the external auditor
  - To review and monitor the external auditor's independence and effectiveness
  - To develop and implement policy on engagement of the external auditor to supply non-audit services
  - To review the risk situation, and to monitor risk-management processes

The Chairman of the audit committee must be independent director with financial expertise.

**Principle 13: The board should undertake periodic appraisal of its own performance and that of each individual director.**

**Key points:**

- *The rigor and formality of the appraisal techniques utilized by the board should reflect the size and complexity of the enterprise.*
- *The chairman should use the appraisal process to obtain feedback on the effectiveness of his/her management of the board.*
- *Group appraisal should examine how the board operates as a collective decision-making body.*
- *Individual appraisal should aim to show whether each director continues to contribute effectively and to demonstrate commitment to the role (including commitment of time).*
- *The chairman should act on the results of the appraisal by recognizing the strengths and addressing the weaknesses of the board, and where appropriate, proposing new members to be appointed to the board or seeking the resignation of directors.*
- *Special attention should also be paid to the assessment of the collaboration of the board as a whole with the management.*

**Notes to Principle 13:**

- *Some of the key questions that an appraisal should address include the following:*
  - Is the distribution of power in the boardroom appropriate?
  - Is there sufficient challenge of executive management in board meetings?
  - Does the board have the right balance between expertise and independence?
  - Does the board correctly perform its duties? Are directors setting direction (guidance and advice on strategy) and monitoring the company (control and risk management) and its management?
  - Do the board members devote sufficient time and effort to the company and their boardroom role?
  - Do board members have adequate access to information and advice?
  - Does the board fully engage sufficiently with shareholders and key stakeholders?
  - Are there personal factors that might inhibit individual board members from fulfilling their duties in an independent and objective manner?

**Principle 14: The board should present a balanced and understandable assessment of the company's position and prospects for stakeholders, and establish a suitable program of stakeholder engagement.**

**Key points:**

- *The board should publish an annual report that is tailored to the needs of its shareholders and its other stakeholders, including employees, creditors and public at large.*

**Notes to Principle 14:**

- *The annual reports may include information on the following corporate issues:*
  - Financial information
  - A statement on company's business model, its vision and values
  - An outline of the company's business strategy and the likely risks associated with that strategy

- A review of the company's activities and performance, and forward-looking assessment of its business environment
- A statement on its corporate governance principles and the extent to which it has complied with the specific corporate governance code, with additional governance information, such as:
  - A statement of how the board operates, including a high-level statement of which types of decisions are to be taken by the board and which are to be delegated to management; the number of its meetings and the participants.
  - The details such as the name, year of birth, education and training, main occupation, essential working experience, date of election to the board of directors, most important simultaneous positions of holdings of the company's shares, holdings and rights based on a share-related and compensation system of the company of all directors, including the chairman, the Administrator (CEO) and members of the board committees (if relevant) of the non-managing directors whom the board determines as independent, with reasons for the assessment where necessary;
  - The names of all directors, including the chairman, the Administrator (CEO) and the chairmen and members of the board committees (if relevant)
  - The names of the non-managing directors whom the board determines as independent, with reasons for the assessment where necessary;
  - Details of how any appraisal of the board, its committees, and its directors has been conducted.
- A summary of activities and projects of special relevance to stakeholders.

Publication of financial key figures in the website of the company may increase shareholders' and public confidence in the company.