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Overview of the Nigerian Code of Corporate Governance for Public Companies 2011

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Introduction

The financial crisis that began in mid-2007 triggered widespread reforms in several countries and internationally. Corporate governance systems were mostly criticised for failing to reduce the impact of the crisis. Following the crisis, the United Kingdom ("the UK") authorities asked Sir David Alan Walker to undertake a review of the UK corporate governance for banks and other financial institutions. The UK Corporate Governance Code[1] was subsequently adopted to replace the Combined Code for listed companies. On the other side of the Atlantic, the United States of America ("the US") responded with the Dodd-Frank Act 2010,[2] which established new rules for shareholder approval of executive compensation and the "golden parachute" compensation arrangements. The US Securities and Exchange Commission adopted these arrangements in its Final Rules on January 25, 2011.[3]

Internationally, the Basel Committee on Banking Supervision responded with its Basel III reform measures in October 2010. The Committee identified six key areas as requiring the greatest focus in corporate governance for banks, including board practices, senior management, risk management and internal controls, compensation, complex or opaque corporate structures, and disclosure and transparency.

[1] June 2010.
[2] The Dodd-Frank Wall Street Reform and Consumer Protection Act 2010.
[3] Set to take effect on April 4, 2011 and made applicable to public companies, with a two-year deferral period for smaller reporting companies.

Nigeria was not left out in these reform measures. In the wake of the financial crisis, the Nigerian Securities and Exchange Commission ("SEC") inaugurated a national committee to review the 2003 Code of Corporate Governance and recommend ways of ensuring compliance by public companies in line with international best practices. The Committee's recommendations formed the basis of the Nigerian Code of Corporate Governance for Public Companies 2011 ("the Code").[4]

The Code will be analyzed in two editions, the first being the current edition of our newsletter. This edition presents an overview of the provisions of the Code, while a subsequent edition will examine the implications of some of its provisions in comparison with the UK and US trends.

HIGHLIGHTS OF THE CODE

The Code is anchored on five main principles:

1. **Leadership**: The Code defines the role of the Board of Directors of public companies ("the Board") and its respective members. It imposes on the Board the responsibility of ensuring the success of the company.
2. **Effectiveness**: The Code requires the Board and its committees to have the appropriate balance of skills, experience and independence to ensure the success of the company.
3. **Accountability**: The Code imposes on the Board the role of presenting a true and fair assessment of the company to its shareholders, stakeholders, the general public, as well as to SEC. The Board is also required to determine the level of risk the company should take to achieve its objectives, as well as establish appropriate risk management and audit frameworks. The Code also requires Board to implement whistle-blowing policies.
4. **Remuneration**: The Board is required to fix the levels, policy and procedure for remuneration of its executive and non-executive members.
5. **Relationship with shareholders**: The Board is required to ensure adequate interactions between management and shareholders. The Code grants institutional and controlling shareholders the power to demand the Board's compliance.

1. Leadership

a) Role of the Board

The Code stipulates that the principal objective of the Board must be to ensure that the company is properly managed.[5] To this end, the Board is responsible for the performance and affairs of the company and should oversee management performance in order to protect and enhance shareholder value. The Board is also charged with the responsibility of ensuring compliance with corporate governance requirements. It may delegate its duties to the Management within defined frameworks, but will at

[4] The Code is made applicable only to public companies. However, SEC encourages other companies not covered by the Code to adopt its principles in the conduct of their affairs.

[5] Section 2 of the Code

times be held responsible for the company's performance.

In addition to the above, the Board has the overall responsibility of:

a) Succession planning and appointment, training, replacement and remuneration of Board members and senior management;
b) Overseeing the effectiveness and adequacy of internal control systems;
c) Overseeing the maintenance of the company's communication and information dissemination policy;
d) Performing appraisals and compensating Board members and senior executives;
e) Ensuring effective communication with shareholders;
f) Ensuring the integrity of financial reports;
g) Ensuring that ethical standards are maintained;[6] and
h) Ensuring compliance with laws.

b. Officers of the Board

i) The Chairman

The Chairman of the Board should be a non-executive director[7] and his primary responsibility would be to ensure the effective operation of the Board towards achieving the company's strategic objectives. The Chairman is also required to refrain from engaging in the day-to-day operations of the company.

The Code requires that for all public companies with listed securities, the positions of the Chairman and Chief Executive Officer (CEO) should be separate and held by different individuals.[8]

ii) The Chief Executive Officer/Managing Director

The CEO or Managing Director (MD) should be the head of the management team and answerable to the Board.[9] The CEO/MD must be knowledgeable in relevant areas of the company's activities. The authority of the CEO/MD and the relationship between the office and the Board should be clearly and adequately described in a letter of appointment. The CEO/MD should ensure the establishment of a culture of integrity and legal compliance which should be imbibed by personnel at all levels of the company.

iii) Executive Directors

The Code requires Executive directors to be knowledgeable in relevant areas of the company's activities in addition to possessing such other qualifications as may be required for their specific assignments or responsibilities. In particular, they should be responsible for the departments they head and should be answerable to the Board through the CEO/MD.

[6] See Part I section 36 of the Code for the requirement for a Code of Ethics and Board's compliance with the Code.
[7] Section 5.1
[8] Section 5.1(b)
[9] Section 5.2

iv) Non-Executive Directors

Non-executive directors should bring independent judgment, as well as necessary scrutiny to the proposals and actions of the management and executive directors, especially, on issues of strategy, performance evaluation and key appointments.

v) Independent Directors

The Code mandates every public company in Nigeria to have a minimum of one independent director on its Board. An independent director is defined as a non-executive director who "is free of any relationship[10] with the company or its management that may impair, or appear to impair the director's ability to make independent judgments."

2. Effectiveness

a) Composition of the Board

The Board should be of a sufficient size relative to the scale and complexity of the company's operations and be composed in such a way as to ensure diversity of experience without compromising independence, compatibility, integrity and availability of members to attend meetings.

The Board should comprise a combination of executive and non-executive directors, majority of whom will be non-executive directors, with at least one independent director.

The Code requires Board members to be individuals with upright personal characteristics, relevant core competences and entrepreneurial spirit, who are committed to the task of good corporate governance.

Membership of the Board should not be less than five.

b) Multiple Directorships

The Code places no limit on the number of concurrent directorships a director may hold. However, it requires the Board and shareholders to carefully consider a director's obligations and commitment in assessing his suitability for appointment into the Board.

c) Family and Interlocking Directorship

The Code restricts the number of Board members with family ties to no more than two. Cross membership on Boards of two or more companies is also disallowed where it would lead to conflict of interest.

d) Board Committees

i) Audit Committee

Section 359(3) and (4) of the Companies and Allied Matters Act (CAMA)[11] requires public companies to have Audit Committees. The Code gives the Board the responsibility of ensuring compliance with statutory requirements and the requirements of the Code.

[10] Including substantial shareholding; section 5.5.

[11] Cap C20 Laws of the Federation of Nigeria, 2004.

ii) Risk Management Committee

The Code allows the Board to establish a Risk Management Committee to assist it in its oversight of the company's risk profile and to establish appropriate risk management framework and risk-reward strategy.

iii) Governance/Remuneration Committee

The Code stipulates that this Committee should be comprised solely of non-executive directors whose duties shall include making recommendations on the compensation structure for executive directors and making input to the company's annual report with respect to directors' compensation, among others.

e) Meetings of the Board

The Code requires the Board to meet at least once every quarter and every director is required to attend at least two-thirds of all Board meetings. Each director's attendance at meetings should form part of the criteria for re-nomination.

f) Appointment to the Board

The Board should develop a written, clearly defined, formal and transparent procedure for appointments to the board of directors. Shareholders should be provided with biographical and all necessary qualification information of proposed directors. A section of the company's annual report should state the processes used in relation to all Board appointments.

g) Performance Evaluation of the Board

The Board should establish a system to undertake a formal and rigorous annual evaluation of its own performance, that of its committees, the Chairman and individual directors. The evaluation system should include the criteria and key performance indicators and targets for the Board, its committees, the Chairman and each individual committee member.

The cumulative result of the performance evaluation of the Board and individual directors should be used as a guide in deciding eligibility for re-election.

h) Development

All directors must receive induction upon joining the company. It is also mandatory for directors to participate in periodic, relevant, professional continuing education programs to update their knowledge and skills.

i) Information and Support

The Chairman is responsible for ensuring that the Board members receive accurate and clear information in a timely manner. The Chairman is responsible for ensuring effective communication and relations with the company's institutional shareholders and strategic stakeholders.

The Company Secretary has the primary duty of assisting the Board and management in implementing the Code and developing good corporate governance practices and culture, as well as facilitating induction and training of new directors.

j) Re-election

Subject to satisfactory performance and the provisions of CAMA,[12] all directors should submit for re-election at regular intervals of at least once every three (3) years. In order to guide decision of shareholders, names and sufficient biographical details of directors nominated for re-election should be accompanied by performance evaluation results and any other relevant information.

3. Accountability

a) Financial and Business Reporting

The Code requires disclosure beyond statutory requirements.[13] It mandates the CEO and Head of Finance of every public company to provide written certifications that the financial statements represent a true and fair view of the affairs of the company.

The Board should ensure that the company's annual report includes a corporate governance report that conveys clear information on the strength of the company's governance structures, policies and practices.

b) Non-financial reporting and Corporate Social Responsibility (CSR)

The Board is expected to pay adequate attention to the interests of stakeholders such as its employees, host community, consumers and the general public. The Board should recognize corruption as a major threat to business and national development and be committed to transparent dealings.

The Code imposes annual reporting requirements on the Board of the company's compliance with social, ethical, safety, health and environmental policies and practices.[14] Some of these disclosure requirements include the company's policies and strategy for addressing and managing the impact of HIV/AIDS, malaria, and other serious diseases on the company's employees and their families. There is also a disclosure requirement on diversity of staff, employment equity and gender policies and practices, especially with respect to executive level opportunities.

c) Risk Management

The Board is required to ensure that the company's annual report makes sufficient disclosure on accounting and risk management. It should oversee the establishment of a management framework that defines the company's

[12]Section 248 of CAMA stipulates the conditions for re-election of directors; it gives the shareholders power to re-elect or reject directors and appoint new ones at Annual General Meeting.

[13] That is beyond the disclosure requirements in CAMA.

[14] See also Part H section 32 of the Code for disclosure to shareholders, stakeholders and the general public in timely and accurate manner.

risk policy, risk appetite and risk limits and clearly communicate them to employees, so as to ensure integration of risk awareness at all levels of the company.

The Board is required to conduct annual risk assessment of all aspects of the company's business and use the result of the assessment to update its risk management framework.

d) Audit Committee and Auditors

The Code requires that at least one member of the Audit Committee should have knowledge of accounting or financial management. The Board is responsible for ensuring the Committee's compliance with statutory, as well as the Code's requirements. The Board should equally maintain appropriate relationships with internal and external auditors. To ensure the independence of the external audit process, the Code requires rotation of external audit firms and partners, who should be retained for no longer than a continuous period of 10 years and re-appointed for an additional 7 years after their initial 10-year engagement.

The Code requires all companies to have an effective risk–based internal audit function. Where the Board fails to comply with the requirement, it should give sufficient reasons in the company's annual report as to how effective internal processes and systems such as risk management, internal control and the like will be obtained.

e) Whistle Blowing Policy

Each company should have a whistle-blowing policy which should be known to employees, stakeholders such as contractors, shareholders, job applicants, and the general public. It is the responsibility of the Board to implement such a policy and to establish a whistle-blowing mechanism for reporting any illegal or substantial unethical behaviour.

4. Remuneration

a) Levels and Components of Remuneration

The Code requires that the levels of remuneration should be sufficient to attract, motivate and retain skilled and qualified persons needed to run the company successfully.

The Board is required to individually approve the remuneration of each executive director including the CEO, taking into consideration direct relevance of the director's skills and experience to the company at the time. On the other hand, the compensation for non-executive directors (NEDs) should be fixed by the Board and approved by shareholders in a general meeting. Such fees, allowance, or other incentives to NEDs and linked to corporate performance should be restricted so as not to compromise their independence.

b) Policy and Procedure

Each company remuneration policy should define the criteria and mechanism for determining the levels of remuneration and frequency of review. It should also define the process for determining executive and NEDs' compensation, and provide how and to what extent executive directors' reward should be linked to corporate and individual performance.

Only NEDs should be involved in decisions regarding remuneration of executive directors.

5. Relations with Shareholders

a) Interactions with shareholders

The Board should ensure that shareholders are treated fairly and given equal access to information about the company. The Board should also ensure that the shareholders' statutory and general rights are protected at all times, and that decisions reached at general meetings are properly and fully implemented.

Institutional and controlling shareholders of companies are expected to demand the Board's compliance with the principles and provisions of the Code. Such institutional and controlling shareholders are expected to seek explanations from the Board in the event of non-compliance. As such, the Board is expected to comply effectively with the provisions of the Code or explain to institutional shareholders and other controlling shareholders the reasons for non-compliance.

b) Annual General Meetings ("AGM")

The Code makes the AGM the primary avenue for meeting and interacting with shareholders. As such, AGMs should be conducted in an open manner allowing for free discussions on all issues on the agenda.

CONCLUSION

This newsletter has outlined the basic provisions of the Nigerian Code of Corporate Governance for Public Companies 2011. Thus, it paves the way for the next edition of our Newsletter which critiques the Code and analyzes its similarities and differences with the US and UK corporate governance systems. The next edition will also examine the extent of the Code's adaptation of the core principles of corporate governance, which the Basel Committee on Banking Supervision proposes.

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