

Annex C

In this annex underlining indicates new text. Text that is not underlined is taken from OSR App4 and its location is referenced by way of a footnote. The numbering used in this chapter is for reference purposes only. It does not indicate the same numbering which will be used if the proposed changes will be inserted into the OSR.



The DFSA Rulebook

Enhanced Corporate Governance Regime for Reporting Entities

APP 1 CORPORATE GOVERNANCE BEST PRACTICE STANDARDS

A1.1 Best practice standards

Guidance

1. App1 contains best practice standards relevant to each of the corporate governance principles set out in chapter 1. The principles in chapter 1 are mandatory, whilst the standards prescribed in this Appendix are examples of practical application of those principles and should be applied taking into consideration the nature (including country of incorporation), size and complexity of a Reporting Entity and its business. For example, it may be too costly for a smaller Reporting Entity to have three separate committees for nomination, remuneration and audit and risk. The Governing Body may choose to combine these committees or perform those functions by itself provided that relevant principles of corporate governance are applied. In the case of a Reporting Entity incorporated in a jurisdiction other than the DIFC, the home jurisdiction may impose different corporate governance requirements which differ from the standards imposed by the DFSA. The Reporting Entity will have to determine if the standards applicable in its home jurisdiction allow it to comply with the DFSA mandatory principles and best practice standards.
2. The standards prescribed are not meant to be exhaustive and a Reporting Entity can implement any additional measures to ensure that its business is run in an adequate and effective manner.
3. A Reporting Entity is required under Rule XX¹ to make a statement in its annual report of how it has applied the best practice standards contained in this Appendix. Where a Reporting Entity departs from any of those standards, it should provide in the annual report an explanation of why it has departed from them it and what other actions, if any, it has taken to ensure compliance with the principles.

Principle 1 – Governing Body

Role of the Governing Body

4. The Governing Body's role should be to provide leadership and control of the Reporting Entity within a framework of prudent and effective controls which enables risk to be assessed and managed.
5. The mandate, composition and working procedures of the Governing Body should be well defined. The Governing Body should make available on the website of the Reporting Entity its written terms of reference.
6. The Governing Body should meet sufficiently regularly within a twelve month period to discharge its duties effectively. There should be a formal schedule of matters specifically reserved for its decision.
7. The Governing Body should set the Reporting Entity's strategic aims, ensure that the necessary financial and human resources are in place for the Reporting Entity to meet its objectives, and review management performance. The Governing Body should set the Reporting Entity's values and standards and ensure that its obligations to its stakeholders are understood and met.
8. As part of their role as members of a Governing Body, non-executive Directors should constructively challenge and help develop proposals on strategy. Non-executive Directors should scrutinise the performance of management in meeting agreed goals and objectives and monitor the reporting of performance. They should satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are robust and effective.

¹ This Rule will be drafted and consulted upon at a later stage

Governing Body Balance and Independence

9. The Governing Body should be of sufficient size that the balance of skills, independence and experience is appropriate for the requirements of the business and that changes to the Governing Body's composition can be managed without undue disruption.
10. The Governing Body should include a balance of executives and non-executives (including independent non-executives) such that no individual or small group of individuals can dominate the Governing Body's decision making.² At least one third of the Governing Body should comprise non-executive Directors, of which at least two non-executive Directors should be independent.³
11. The Governing Body should consider a non-executive Director to be "independent" if the Director is found, on the reasonable determination by the Governing Body, to be independent in character and judgement and have no relationships or circumstances which are likely to affect or could appear to affect the Director's judgement in a manner other than in the best interests of the Reporting Entity. In forming a determination, the Governing Body should consider the following:
 - a. the length of time the Director has served as a member of the Governing Body;
 - b. whether the Director has been an employee of the Reporting Entity or group within the last five years;
 - c. whether the Director has or has had, within the last three years, a material business relationship with the Reporting Entity, either directly or as a partner, shareholder, Director or senior employee of a body that has such a relationship with the Reporting Entity;
 - d. whether the Director receives or has received, in the last three years additional remuneration or payments from the Reporting Entity apart from a Director's fee, participates in the Reporting Entity's share option, or a performance-related pay scheme, or is a member of the Reporting Entity's pension scheme;
 - e. whether the Director is or has been a Director, partner or employee of a firm which is the Reporting Entity's auditor;
 - f. whether the Director has close family ties with any of the Reporting Entity's advisors, Directors or senior employees;
 - g. whether the Director holds cross Directorships or has significant links with other Directors through involvement in other companies or bodies; or
 - h. whether the Director represents a significant shareholder.⁴

Appointment to the Governing Body

12. There should be a formal, rigorous and transparent procedure for the appointment of new Directors to the Governing Body.
13. Appointments to the Governing Body should be made on merit and against objective criteria. Care should be taken to ensure that appointees have enough time available to devote to the job. This is particularly important in the case of chairmanships.
14. All Directors should be submitted for re-appointment at regular intervals, subject to continued satisfactory performance. The Governing Body should ensure planned and progressive refreshing of the Governing Body. All Directors should be subject to election by shareholders

² A4.3.2 Guidance 1

³ A4.3.2 with minor amendments

⁴ A4.3.2 with minor amendments

at the first annual general meeting after their appointment, and to re-election thereafter at intervals of no more than three years.

15. The Governing Body should satisfy itself that plans are in place for orderly succession for appointments to the Governing Body and to senior management, so as to maintain an appropriate balance of skills and experience within the Reporting Entity and on the Governing Body.

Nomination Committee

16. There should be a nomination committee which should lead the process for appointments and make recommendations to the Governing Body. A majority of members of the nomination committee should be independent non-executive Directors. The chairman of the nomination committee should be an independent non-executive Director.
17. The mandate, composition and working procedures of the nomination committee should be well defined. The nomination committee should make available on the website of the Reporting Entity its written terms of reference explaining its role and the authority delegated to it by the Governing Body.⁵
18. The nomination committee should evaluate the balance of skills, knowledge, independence and experience on the Governing Body and, in the light of this evaluation, prepare a description of the role and capabilities required for a particular appointment.⁶
19. For the appointment of a chairman, the nomination committee should prepare a job specification, including an assessment of the time commitment expected, recognising the need for availability in the event of crises. A chairman's other significant commitments should be disclosed to the Governing Body before appointment and included in the annual report. Changes to such commitments should be reported to the Governing Body as they arise, and their impact explained in the next annual report.
20. The terms and conditions of appointment of non-executive Directors should be made available for inspection on the Reporting Entity's website. The letter of appointment should set out the expected time commitment. Non-executive Directors should undertake that they will have sufficient time to meet what is expected of them. Their other significant commitments should be disclosed to the Governing Body before appointment, with a broad indication of the time involved and the Governing Body should be informed of subsequent changes.

Performance evaluation

21. The Governing Body should undertake a formal and rigorous annual evaluation of its own performance and that of its committees and individual Directors.
22. The chairman should act on the results of the performance evaluation by recognising the strengths and addressing the weaknesses of the Governing Body.

Remuneration

23. Levels of remuneration of Directors should be sufficient to attract and retain ~~the~~ Directors of the quality needed to serve the Reporting Entity successfully, but the Reporting Entity should avoid paying more than is necessary for this purpose. An appropriate proportion of executive Directors' remuneration should be structured so as to link rewards to corporate and individual performance.⁷
24. The performance-related elements of remuneration should form an appropriate proportion of the total remuneration package of executive Directors and should be designed to align their

⁵ A4.3.7 Guidance 2

⁶ A4.3.7 Guidance 3

⁷ A4.3.7 Guidance 8

interests with those of shareholders and to give these Directors keen incentives to perform at the highest levels.

25. Levels of remuneration for non-executive Directors should reflect the time commitment and responsibilities of the role. Remuneration for non-executive Directors should not include share options unless shareholder approval is sought in advance and any shares acquired by exercise of the options should be held until at least one year after the non-executive Director leaves the Governing Body.
26. There should be a formal and transparent procedure for developing policy on executive remuneration and for fixing remuneration packages of individual Directors. No Director should be involved in deciding his own remuneration.⁸

Remuneration Committee

25. The Governing Body should establish and maintain a remuneration committee to assess the remuneration of Directors (including the chairman).⁹ It should comprise at least three independent non-executive Directors. In addition, the chairman of the Governing Body may also be a member but not the chair of the committee.
26. The remuneration committee should have delegated responsibility for setting remuneration for all executive Directors and the chairman. The committee should also recommend and monitor the level and structure of remuneration for senior management.¹⁰ The definition of “senior management” for this purpose should be determined by the Governing Body but should normally include the first layer of management below the Governing Body.
27. The mandate, composition and working procedures of the remuneration committee should be well defined. The remuneration committee should make available on the website of the Reporting Entity its written terms of reference explaining its role and the authority delegated to it by the Governing Body.¹¹
28. The remuneration committee should also be responsible for appointing any consultants in respect of executive Director’s remuneration.
29. The Governing Body itself, or where required by the articles of association or other constituent documents, the shareholders, should determine the remuneration of the non-executive Directors.

Principle 2 – Division of responsibilities

30. No one individual should have unfettered powers of decision. The division of responsibilities should be clearly established, set out in writing and agreed by the Governing Body.¹²
31. The chairman should be responsible for leadership of the Governing Body, ensuring its effectiveness on all aspects of its role and setting its agenda.¹³
32. The roles of the chairman and chief executive should not be exercised by the same individual.¹⁴
33. A chief executive should not go on to be the chairman of the same Reporting Entity.
34. The chairman should on appointment meet the independence criteria set out in Guidance 11.

⁸ A4.3.7 Guidance 6

⁹ A4.3.7 Guidance 4 with minor amendments

¹⁰ A4.3.7 Guidance 5

¹¹ A4.3.7 Guidance 8

¹² A4.3.2 Guidance 5 with minor amendments

¹³ A4.3.2 Guidance 6

¹⁴ A4.3.2 Guidance 6 with minor amendments

Principle 3 – Systems of management

35. The Governing Body should, at least annually, conduct a review of the effectiveness of the Reporting Entity's systems of management and internal controls and should report to the shareholders that it has done so. The review should cover all aspects of material controls, including management, financial, operational and compliance controls and risk management systems. The Governing Body may satisfy this requirement by instructing an external auditor to undertake the review and report to it on its outcome.¹⁵
36. The Governing Body should establish formal and transparent arrangements for considering how it should apply the financial reporting and internal control principles and for maintaining an appropriate relationship with its auditors.
37. The Governing Body should establish policies and procedures for the identification and oversight and management of material business risks and disclose a summary of those policies and procedures. The Governing Body should ensure that management implements the requisite risk management and internal control systems to manage material business risks.

Audit Committee

38. A Governing Body should establish and maintain an audit committee to monitor and review the Reporting Entity's internal audit function¹⁶ and other internal controls. The terms of reference of the committee should include at least the following¹⁷:
- monitoring the integrity of the financial statements of the Reporting Entity and any formal announcements relating to the Reporting Entity's financial performance and reviewing significant financial reporting judgements contained in them;
 - reviewing the Reporting Entity's internal financial controls and, unless expressly addressed by a separate risk committee of the Governing Body or the Governing Body itself, internal controls and risk management systems;
 - monitoring and reviewing the effectiveness of the Reporting Entity's internal audit function;
 - making recommendations to the Governing Body in respect of the appointment, re-appointment, removal and terms of engagement, including remuneration, of the external auditor;
 - reviewing and monitoring the external auditor's independence and objectivity and the effectiveness of the audit process; and
 - developing and implementing policy on the engagement of the external auditor to supply non -audit services.
39. The mandate, composition and working procedures of the audit committee should be well defined. The audit committee should make available on the website of the Reporting Entity its written terms of reference explaining its role and the authority delegated to it by the Governing Body.¹⁸
40. A Governing Body should appoint at least two independent non-executive Directors to that committee.¹⁹ At least one of the independent non-executive Directors appointed to the audit committee should have financial expertise.²⁰ The chair of the audit committee should be an independent non-executive Director.

¹⁵ A4.3.9 Guidance 1 with minor amendments

¹⁶ A4.3.8 (a) with minor amendments

¹⁷ A4.3.8 Guidance 2 with minor amendments including a. to f.

¹⁸ A4.3.8 Guidance 2

¹⁹ A4.3.8 (b)

²⁰ A4.3.8 Guidance 1

41. The audit committee should review arrangements by which staff of the Reporting Entity may, in confidence, raise concerns about possible improprieties in matters of financial reporting or other matters. The audit committee's objective should be to ensure that arrangements are in place for the proportionate and independent investigation of such matters and for appropriate follow-up action.

Principle 4 – Rights of shareholders

42. The Governing Body as a whole has responsibility for ensuring that a satisfactory dialogue with shareholders takes place. Such dialogue should be based on the mutual understanding of objectives.
43. A Governing Body should use the annual general meeting to communicate with shareholders and encourage their participation. Shareholders should have the opportunity to ask questions of the Governing Body, to place items on the agenda of general meetings and to propose resolutions.²¹
44. At any general meeting, the Reporting Entity should propose a separate resolution on each substantially separate issue, and should in particular propose a resolution at the annual general meeting relating to the report and accounts. For each resolution, proxy appointment forms should provide shareholders with the option to direct their proxy to vote either for or against the resolution or to withhold their vote.
45. The chairman should arrange for the chairmen of the audit, remuneration, and nomination committees to be available to answer questions at the annual general meeting and for all Directors to attend either in person or by electronic means.
46. Whilst recognising that most shareholder contact is with the chief executive and finance Director, the chairman and other Directors as appropriate should maintain sufficient contact with major shareholders to understand their issues and concerns. The Governing Body should keep in touch with shareholder opinion in whatever ways are most practical and efficient.
47. The chairman should ensure that the views of shareholders are communicated to the Governing Body as a whole. In addition, the chairman should discuss governance and strategy with major shareholders. Non-executive Directors should be offered the opportunity to attend meetings with major shareholders and should expect to attend them if requested by major shareholders.
48. The Governing Body should ensure that no steps are taken which may prevent shareholders consulting with other shareholders on issues concerning their basic shareholder rights, subject to exceptions to prevent abuse.²²
49. The Governing Body should use its website as a forum for the posting of information such as new strategies, calendar for important meetings and other events.
50. The Governing Body should protect minority shareholders from any oppressive or abusive action by controlling shareholders.²³

Principle 5 – Supply of information

51. The chairman is responsible for ensuring that the Directors receive accurate, timely and clear information. Senior management has an obligation to provide such information, but Directors should seek clarification or amplification where necessary.
52. The chairman should ensure that the Directors continually update their skills and the knowledge and familiarity with the Reporting Entity required to fulfil their role both on the Governing

²¹ A4.3.3 Guidance 1

²² A4.3.3 Guidance 3

²³ A4.3.3 Guidance 4 with minor amendments

Body and its committees. The Reporting Entity should provide the necessary resources for developing and updating its Directors' knowledge and capabilities. The chairman should ensure that new Directors receive an appropriate induction on joining the Governing Body.

53. Under the direction of the chairman, the Reporting Entity's secretary's responsibilities include ensuring good information flows within the Governing Body and its committees and between senior management and non-executive Directors, as well as facilitating induction and assisting with professional development as required. The Reporting Entity's secretary should be responsible for advising the Governing Body through the chairman on all governance matters.
54. All Directors should have access to the advice and services of the Reporting Entity's secretary, who is responsible to the Governing Body for ensuring that Governing Body procedures are complied with. Both the appointment and removal of the Reporting Entity's secretary should be a matter for the Governing Body as a whole.
55. The Governing Body should ensure that Directors, especially non-executive Directors, have access to independent professional advice at the Reporting Entity's expense where they judge it necessary to discharge their responsibilities as Directors. Committees should be provided with sufficient resources to undertake their duties.

Principle 6 –Position and Prospects

56. The Reporting Entity's responsibility to present a true, balanced and understandable assessment should extend to interim and other price-sensitive public reports and reports to regulators as well as to information required to be presented by law.²⁴

²⁴ A4.3.9 Guidance 2 with minor amendments