



CENTRAL BANK OF  
TRINIDAD & TOBAGO

# Corporate Governance Guideline

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## Table of Contents

1.	INTRODUCTION	1
2.	PURPOSES OF GUIDELINE	1
3.	APPLICATION AND SCOPE	2
4.	DEFINITIONS OF KEY TERMS	2
5.	FRAMEWORK USED BY CENTRAL BANK TO ASSESS CORPORATE GOVERNANCE	3
6.	COMPOSITION OF THE BOARD	3
7.	THE BOARD'S ROLE AND FUNCTION	4
8.	THE AUDIT COMMITTEE	7
9.	THE CONDUCT REVIEW COMMITTEE	8
10.	THE COMPENSATION COMMITTEE	8
11.	THE NOMINATION COMMITTEE	8
12.	THE RISK MANAGEMENT COMMITTEE	9
13.	SUCCESSION PLANNING	10
14.	BOARD MEETINGS	11
15.	GOVERNANCE OF CONGLOMERATES/CORPORATE GROUPS	12
16.	THE RELATIONSHIP BETWEEN THE BOARD AND THE CENTRAL BANK	13

## CORPORATE GOVERNANCE GUIDELINE

### 1. INTRODUCTION

1.1 Financial institutions play a crucial role in the development and stability of every economy. They are responsible for the efficient transfer of funds from consumers/savers to productive sectors of the economy via loans and investments. To remain competitive in an increasingly global environment, financial institutions have embarked on expansion initiatives, often outside their home jurisdiction. The significance of these expansionary activities is that failure of financial institutions may create systemic problems in both domestic and foreign jurisdictions. In addition, financial institutions, quite unlike other corporate entities that rely on shareholder equity, depend on deposits in the case of the banking sector and policyholders' funds in the case of insurance companies as major sources of funding. These characteristics underscore the importance of strong corporate governance in financial institutions.

1.2 Corporate Governance refers to the framework by which the Board and Senior Management of organizations are held accountable for the operations of the institutions they oversee. This framework encompasses the mechanisms, structures and processes that enable the Board of Directors to set the objectives and strategies of the institution, monitor and evaluate its performance, and take corrective action promptly. Good corporate governance therefore, requires that the relationships among management, the Board, shareholders, regulators and other stakeholders are transparent, fair and well balanced.

### 2. PURPOSES OF GUIDELINE<sup>1</sup>

2.1 The purposes of this Guideline are to ensure that (a) the Board of Directors and Senior Management of these institutions are fully cognizant of the need to adopt sound principles and practices for the internal governance of the institutions they oversee, and (b) institutions are aware of the factors considered by the Central Bank in assessing corporate governance practices.

2.2 This Guideline will be updated periodically to ensure continued relevance as corporate governance practices evolve. Nevertheless, the Central Bank expects the Board<sup>2</sup> and Senior Management of financial institutions to keep abreast of developments in this area and to adopt best practices with respect to their oversight responsibilities.

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<sup>1</sup> In developing this Guideline the Central Bank has considered relevant legislation as well as best practices as enunciated by the international regulatory agencies. In addition, corporate governance guidelines in other jurisdictions have been examined.

<sup>2</sup> The term "Board" is used to refer either to the Board of Directors or the Board Committees that have been authorised to oversee a particular function.

### 3. APPLICATION AND SCOPE

3.1 In this Guideline, a financial institution refers to (i) institutions licensed under the Financial Institutions Act, 1993 (FIA) (ii) institutions and persons registered under the Insurance Act, Chap 84:01 (IA).

### 4. DEFINITIONS OF KEY TERMS

4.1 An *executive director* is a director who is part of the current management team of the institution.

4.2 A *non-executive director* is a director who is not part of the current management of the institution.

4.3 An *independent director* is a director who:-

4.3.1 *Has not been employed by the financial institution or any of its connected or related parties within the past three years.*

4.3.2 *Is not a substantial shareholder (10%) of a listed financial institution or a controlling person of a non-listed financial institution (or member of a group of individuals and/or entities that collectively exercise control over the financial institution), or otherwise associated directly or indirectly with a substantial shareholder or controlling person of a financial institution.*

4.3.3 *Is not a company, or is not connected to a company that provides material advice or consultancy to the financial institution or its connected or related parties. **The nature of the advice or consultancy provided would not be considered material if it does not impact the critical operations of the financial institution.***

4.3.4 *Is not involved in any material business arrangement with the financial institution. Business arrangements are not considered material and are not likely to jeopardize the director's judgment and thereby his independence if: -*

- *The arrangements are usually and customarily offered to customers of the financial institution;*
- *The arrangements are offered on substantially similar terms as those prevailing at the time for comparable transactions with other customers under similar circumstances;*
- *In the event that (i.) a proposed arrangement were not made or (ii.) an existing arrangement were terminated in the normal course of business, that action would not reasonably be expected to have a material and adverse effect on the financial institution's financial condition, results of operations, or the business of the proposed director;*

4.3.5 *Is not a member of the immediate family of an individual who is, or has been during the past two years employed by the financial institution.*

4.3.6 *Is not, nor in the past two years has been, affiliated with, or employed by a present or former auditor of the financial institution, or any of the auditor's connected or related parties.*

## 5. FRAMEWORK USED BY CENTRAL BANK TO ASSESS CORPORATE GOVERNANCE

5.1 The Central Bank assesses the corporate governance of financial institutions by evaluating the structure of the Board and the oversight functions of both the Board and Senior Management. An assessment of the oversight function is conducted with a view to determining the capability of the Board and Senior Management in ensuring that the financial institution is operating in a safe and sound manner, including compliance with applicable laws and regulation. Assessment of the oversight function would therefore cover, inter alia, the following areas:

- The Board's understanding and working knowledge of the types of risks inherent in an institution's activities;
- The Board's review and approval process of the policies and procedures, which guide the operations of the institution, including its involvement in determining acceptable risk exposure levels for the institution;
- The Board's participation in setting the strategic direction of the institution;
- Senior Management's knowledge and experience and whether this is consistent with the nature and scope of the institution's activities;
- The tools used by Senior Management in identifying, measuring and monitoring the risks of the institution.

## 6. COMPOSITION OF THE BOARD

6.1 The Board of an institution should comprise both executive and non-executive directors, at least two of whom should be independent. Licensees and registrants which do not currently satisfy this requirement would be allowed a transition period of up to three years from the date of issue of this guideline to comply.

6.2 It is desirable that the Chairman of the Board and the Chief Executive Officer (CEO) or Managing Director of the institution be separate individuals. As far as possible, where the offices of the Chairman and the CEO or Managing Director are held by different people, there should be a clear division of responsibilities.

- 6.3 Additionally, the Board should comprise persons who are fit and proper<sup>3</sup>. For example, directors should have the appropriate experience and/or skill; should not have been convicted of a crime; should not have been dismissed or asked to resign over financial or other impropriety; should conduct their financial affairs in a sound manner; and should be persons of integrity.
- 6.4 A director of a financial institution or of its holding company shall not be a director of: (a) any other financial institution or (b) the holding company of any other financial institution

## 7. THE BOARD'S ROLE AND FUNCTION

- 7.1 In order for the Board to perform effectively, directors should exercise the required care<sup>4</sup>, diligence and skill that a reasonable prudent person would exercise in comparable circumstances. It is also desirable that Board members demonstrate independent thinking and sound judgment. This would ensure that no one director or block of directors dominates the Board's decision making and that active participation by all is encouraged. Decisions taken should be informed by reasonable and balanced assessments of all relevant information.
- 7.2 The Board should develop an appropriate and comprehensive framework to govern the operations of the financial institution. Such a framework should require the Board to: -
- 7.2.1 *Establish business objectives and provide strategic guidance. Accordingly, a management information system should be so structured to enable timely critical decision-making;*
  - 7.2.2 *Ensure that the CEO or Managing Director and other senior officers of the financial institution are qualified and competent with sufficient experience and knowledge of the business and that succession planning is in place for these and other positions deemed critical to the organization;*
  - 7.2.3 *Consider using the supervisory recommendations as one of the inputs in assessing the effectiveness of Senior Management;*
  - 7.2.4 *Approve the financial institution's policies for major activities, such as loans, liquidity, investment and insurance underwriting;*
  - 7.2.5 *Approve the compensation of members of senior management and other key personnel and ensure that the compensation is consistent with the financial institution's culture, objectives, strategies and control environment;*
  - 7.2.6 *Ensure that Senior Management has documented policies and procedures to ensure that activities are undertaken in accordance with the approved business strategy;*
  - 7.2.7 *Be satisfied that the information technology systems are appropriate and reinforced with a system of checks and balances to enforce trustworthiness of data;*
  - 7.2.8 *Approve the financial institution's control framework and ensure that these controls are operating efficiently;*

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<sup>3</sup> See the Fit and Proper Guideline issued by the Central Bank for details on assessing the fitness and propriety of directors.

<sup>4</sup> See Companies Act Section 99.

- 7.2.9 *Understand the significant risks to which the financial institution is exposed and ensure that there is an effective risk management system in place<sup>5</sup>;*
- 7.2.10 *Understand the statutory obligations with which the financial institution must comply and ensure that there is an effective compliance system in place for all applicable laws and regulations;*
- 7.2.11 *Monitor financial performance;*
- 7.2.12 *Establish standards of business conduct and ethical behaviour for directors, senior management and other personnel of the organization. Therefore, the Board should ensure that Senior Management implements policies that are fair, and address conflicts of interest, lending to officers and employees and other forms of self-dealing, and preferential treatment to connected parties and other favoured entities. Processes should be established that allow the Board to monitor compliance with these policies and ensure that deviations are reported to an appropriate level of management;*
- 7.2.13 *Communicate with the supervisory authority and convene meetings when requested;*
- 7.2.14 *Be informed of and review reports and recommendations of the supervisory authority and ensure that such recommendations are implemented;*
- 7.2.15 *Conduct periodic self-assessments.*
- 7.3 The Board must continuously assess the performance of the financial institution to ensure that expectations and the established framework (see 7.2) remain appropriate. The Board's activities should include regular review of business objectives and strategies, financial statements and Audit Committee findings. The Board should also continuously evaluate the effectiveness of Senior Management.
- 7.4 The Board also has a duty to ensure transparency by promptly communicating with shareholders any developments that may impact shareholder value such as: -
- 7.4.1 *The operations and financial condition of the institution;*
- 7.4.2 *Significant and material information;*
- 7.4.3 *Certain proposals for which directors should obtain their approval, such as stock options for directors and changes in voting rights for classes of shares;*
- 7.4.4 *All shareholders' agreements that would influence the investment decisions.*
- 7.5 The Board may delegate functions to the Senior Management of the organization or to its Committees. However, the entire Board remains ultimately responsible for directing and overseeing the performance of the financial institution.

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<sup>5</sup> Refer to section 12.1.1 of this Guideline.

### 7.5.1 *The Role of Senior Management*

- *The primary responsibility of Senior Management is to manage the day to day operations of the financial institution in accordance with the objectives and policies set out by the Board.*
- *Senior Management of the institution should also provide the Board with comprehensive, relevant, timely and accurate information to facilitate informed decision making.*

*Senior Management enhances Board effectiveness by:-*

- *Providing the Board with recommendations for achieving the strategic direction of the institution.*
- *Ensuring that the independent oversight functions (internal audit and risk management) have adequate resources to fulfill their mandates such that there is the capacity to present objective opinions and advice to the Board.*

*Senior Management is directly responsible for:-*

- *Developing annual operating plans and budgets.*
- *The integrity of the financial reporting system and the preparation of financial reports.*
- *Appropriate follow-up and implementation of the recommendations of the on-site examination process.*

### 7.5.2 *The Nature and Operations of Board Committees*

- *Board Committees are established to undertake specific functions and make recommendations to the Board. Notable Board Committees include an Audit Committee, a Conduct Review Committee, a Risk Management Committee, a Compensation Committee and a Nomination Committee. Of these, **only the Audit Committee is required**<sup>6</sup> however an institution may wish to establish one or more of the other committees depending on the size and level of complexity of its operations.*

*Each Committee must have a charter that details the following: -*

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<sup>6</sup> The Central Bank has proposed amendments to the FIA to make the Audit Committee mandatory, comprising at a minimum three directors, and requiring that a majority of committee members and the chairman be independent, notwithstanding Section 157 (1) of the Companies Act Chapter 81:01 with respect to private companies. A similar amendment is expected to be proposed to the Insurance Act.

- *Purpose and objectives;*
- *Responsibilities;*
- *Frequency of and attendance at meetings;*
- *Qualification for membership;*
- *Appointment and removal procedures;*
- *Structure and operations;*
- *Reporting to the Board.*

## 8. THE AUDIT COMMITTEE

8.1 Each financial institution should establish an Audit Committee which should comprise a minimum of three directors. In addition, the majority of the members of the Audit Committee should be independent and not a connected party. Further, the Chairman of the Audit Committee should be independent.

8.2 The audit committee must play a critical role in monitoring and strengthening the financial institution's control environment and its duties should include: -

*8.2.1 Ensuring that an independent auditing firm is hired to audit the financial statements prepared by management and to issue an opinion on the statements based on internationally accepted accounting standards and local regulatory requirements;*

*8.2.2 Reviewing the annual financial statements and issuing a report to the Board before such statements are approved;*

*8.2.3 Monitoring management and staff compliance with policies, laws, regulations and guidelines;*

*8.2.4 Reviewing investments and transactions that could adversely affect the financial institution;*

*8.2.5 Supervising the audit function to verify that both the internal and external auditors are objective in their assessment and independent of management's influence;*

*8.2.6 Ensuring that the audits conducted are risk-based and comprehensive in scope;*

*8.2.7 Monitoring of management's efforts to correct deficiencies identified by both the internal and external auditors;*

*8.2.8 Ensuring that the risk management function is independent and comprehensive;*

*8.2.9 Meeting with the full Board to consider any matter of urgent concern to the committee;*

*8.2.10 Reviewing such returns of the company that the Central Bank may specify.*

## **9. THE CONDUCT REVIEW COMMITTEE**

9.1 The Board may establish a Conduct Review Committee<sup>7</sup> to institute procedures for reviewing transactions with connected parties, as well as mechanisms for monitoring and reporting such transactions on a continuous basis. The procedures should ensure that all transactions are conducted at "arms length."

## **10. THE COMPENSATION COMMITTEE**

10.1 The Board may establish a Compensation Committee<sup>8</sup> to provide oversight of remuneration of senior management and other key personnel and to ensure consistency with the financial institution's culture, objectives, strategy and control environment. For example, remuneration should not provide incentives for excessive risk-taking nor overly depend on short-term performance, such as short-term trading gains.

10.2 The Compensation Committee should have an independent chair and be composed solely of independent directors.

10.3 This committee should also recommend to the Board the fees to be paid to each non-executive director. The Board should then submit the proposal to shareholders in a general meeting for approval, prior to implementation and payment.

## **11. THE NOMINATION COMMITTEE**

11.1 The Board may establish a Nomination Committee<sup>9</sup> whose function should include self-assessments of Board effectiveness on an annual basis. This committee should also direct the process of renewing and replacing Board members by assessing whether the current

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<sup>7</sup> The Board may establish this Committee to assist it in fulfilling its mandate under Section 7.2.12 of this Guideline.

<sup>8</sup> The Board may establish this Committee to assist it in fulfilling its mandate under Section 7.2.5 of this Guideline.

<sup>9</sup> The Board may establish this Committee to assist it in fulfilling its mandate under Section 7.2.15 of this Guideline.

composition brings adequate diversity of skills, backgrounds, expertise and levels of active participation to further the best interests of the institution.

- 11.2 The committee should consider the core skills and added value nominees are expected to bring to the Board and the resulting composition of the Board, when nominating persons.
- 11.3 The committee should be chaired by an independent director, with the majority of its members also being independent.

## 12. THE RISK MANAGEMENT COMMITTEE

- 12.1 The Board may establish a Risk Management Committee<sup>10</sup> to provide oversight of the senior management's activities in managing credit, market, liquidity, operational, legal, and other risks of the financial institution. One function of such a committee is to keep the Board informed on risk exposures and risk management activities through the submission of periodic reports from senior management.

### *12.1.1 The Role of the Board in Risk Management*

*The Board is entrusted with oversight responsibilities for risk management. Each financial institution should have a risk management process that appropriately manages and mitigates the risks inherent in the types of business conducted, given the size and complexity of its operations. The process may range from centralized to de-centralized<sup>11</sup>, as long as it enables the Board and Senior Management to achieve effective risk management throughout the organization. Risks arising from external sources and group relationships, such as competitors, parent companies, subsidiaries and affiliates, should also be addressed in the risk management process.*

*At a minimum, effective oversight would require the Board to:-*

- *Have a general appreciation of the types of risks to which the financial institution may be exposed and of the techniques used to quantify and manage those risks. This includes an understanding of operating structures*

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<sup>10</sup> The Board may establish this Committee to assist it in fulfilling its mandate under Section 7.2.9 of this Guideline.

<sup>11</sup> Centralized risk management functions aggregate the risks across separate business units and manage them across the entire entity. Decentralized risk management functions involve each business unit focusing solely on its own operations, and managing risk on a transaction by transaction basis.

*such as special purpose vehicles or corporate trusts used as part of the institution's extended business operations;*

- *Review and approve the overall risk philosophy and risk limits of the institution;*
- *Examine and approve policies or changes in policies prior to implementation. Policies should comprehensively address the institution's main activities, and should reflect its risk management objectives;*
- *Ensure that management has a process for determining capital adequacy, given the risks assumed, and for ensuring that capital planning and management strategies are in place;*
- *Ensure that management provides timely and accurate reporting on the key risks faced by the institution, the procedures and controls in place to manage these risks, and the overall effectiveness of risk management practices;*
- *Be informed of, and satisfied with, the manner in which material exceptions to policies and controls within the institution are identified, monitored, and reported to the Board, and the consequences within the institution, when exceptions are identified;*
- *Ensure that the risk management activities of the institution are independent, accorded high priority and reviewed periodically;*
- *Incorporate in its reviews of new business strategies or proposals, an evaluation of required changes in risk management systems.*

## 13. SUCCESSION PLANNING

13.1 Succession practices refer to the nomination, orientation and training of new directors and persons identified as possible successors to senior management and for other critical functions. The Board should have a process for identifying, nominating and retaining qualified directors and senior management. For example, personal qualities such as strength of character, an inquiring and independent mind, sound judgment and attributes such as professional qualification, technical or specialized skills and work experience should be considered.

13.2 The Board should consider instituting a formal program for new directors and persons identified as possible successors to senior management and for other critical functions. This program should cover: -

*13.2.1 Key characteristics and nature of the industry;*

*13.2.2 The financial regulatory system;*

*13.2.3 The institution's strategic plans, operations and management structure;*

*13.2.4 The control structure, including the role of the internal and external auditors;*

*13.2.5 Fiduciary duties and responsibilities of directors.*

13.3 Persons identified as potential successors should be familiar with the laws, regulations, codes and guidelines governing the institution's operations.

13.4 Persons identified in the succession plan should undergo continuous training to ensure that they are updated on new laws, industry developments, emerging trends, products, risks and opportunities.

13.5 The Board should also consider putting a program in place for staggering the terms of directors [unless specified in the by-laws], subject to performance and eligibility for re-election.

## **14. BOARD MEETINGS**

14.1 The full Board must meet at least as frequently as stipulated in the company's articles or by-laws. However, the Central Bank may, based on examination findings, request more frequent meetings of the Board.

14.2 Directors of the Board are expected to attend and actively participate in all meetings of the full Board, as well as meeting of committees and sub-committees of the Board.

14.3 All relevant information such as, but not limited to, the agenda, Board minutes and papers, should be forwarded to all directors prior to the meeting and in sufficient time to allow the documents to be adequately reviewed.

- 14.4 Attendance at meetings must be recorded and it is desirable to note whether attendance was in-person, via telephone or other technologies. Excused absences cannot be considered as attendance.
- 14.5 Minutes should be taken at each meeting of the Board. The minutes must also document the establishment and composition of committees, and note the abstention of any director from any vote. The Board should ensure that the minutes accurately and adequately reflect the decisions and actions taken.
- 14.6 Additionally, at Board meetings, the Chairman should: -
- 14.6.1 Maintain control of proceedings without dominating discussions;*
  - 14.6.2 Stimulate debate by drawing out the contributions of all members;*
  - 14.6.3 Guide discussions while ensuring that genuine disagreements are aired and resolved;*
  - 14.6.4 Ensure decisions reached are properly understood and recorded.*

## 15. GOVERNANCE OF CONGLOMERATES/CORPORATE GROUPS

- 15.1 The Board of the parent company of a financial institution within a financial group must be informed of all material risks and matters that affect the entire group. The Board of the parent company should establish reporting structures for the subsidiaries to ensure that there is adequate oversight of the activities of the subsidiary.
- 15.2 The Board of the parent company should closely monitor the performance, composition and activities of the Boards of subsidiaries, especially where: -
- 15.2.1 The activities of a subsidiary differ significantly or are independent from the core business of the parent;*
  - 15.2.2 Special expertise is required to provide oversight of the subsidiary's activities;*
  - 15.2.3 There is the potential for conflicts of interest between the various stakeholders of the parent and the subsidiary;*
  - 15.2.4 Some of the activities conducted within the group may give rise to material legal and reputational risks for the financial institutions in the group; or*
  - 15.2.5 The subsidiary operates in a jurisdiction that has substantially different expectations of governance that may result in regulatory arbitrage.*
- 15.3 The Board of a financial institution which is a subsidiary or affiliate within a conglomerate/group should:

- 15.3.1 *Review the holding company's policies to ensure that they do not create current or potential risks to the financial institution;*
- 15.3.2 *Be aware of the activities and financial condition of the affiliates in the corporate group and the legislative framework in jurisdictions in which they operate;*
- 15.3.3 *Notify the holding company and discuss modifications, if the holding company practices are found to be either inappropriate or harmful. If concerns remain unheeded, dissent should be recorded and action considered to protect the financial institution;*
- 15.3.4 *Notify the Inspector of Financial Institutions of the impact on the institution of unheeded concerns arising out of the holding company's decisions and activities; and*
- 15.3.5 *Refrain from conducting transactions with connected parties that prejudice the institution such as, but not limited to: -*
  - (i) Acquiring low quality assets
  - (ii) Preferential lending (significantly below market rates)
  - (iii) Paying excessive dividends
  - (iv) Paying unearned or excessive management fees

## **16. THE RELATIONSHIP BETWEEN THE BOARD AND THE CENTRAL BANK**

- 16.1 The Board should understand the regulatory framework under which financial institutions operate and cooperate with the Central Bank in ensuring that the financial system is safe and sound. The Board should therefore: -
  - 16.1.1 *Maintain open communication with the Central Bank on all material issues pertaining to the institution;*
  - 16.1.2 *Comply promptly and fully with requests for information as required by law;*
  - 16.1.3 *Be aware of the findings of the on-site examination process and direct Senior Management to determine whether similar problems exist elsewhere in the institution and take corrective action.*