

LeishTon
A C A D E M Y

The Draft Nigerian Code of Corporate Governance 2018 Key Preliminary Comments

ICAN Stakeholder Dialogue

July 9, 2018

Facilitated by:

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Established Facts



- Suspended National Code of Corporate Governance (NCCG) for Private Sector
- The appointment and inauguration of the Steering Committee for the Development of the NCCG on Thursday January 17, 2013
- The appointment and inauguration of a Technical Committee on the NCCG on Thursday January 18, 2018
- The details of the members of the Steering Committee, including name, contact address, phone number, email addresses and organisation or group being represented were released to the public by the Financial Reporting Council of Nigeria (FRCN) to allow for easy access to members of the committee by the public
- The details of members of the Technical Committee was not found on the FRCN website



Our Understanding of the Terms of Reference – The Steering Committee



- Our understanding of the terms of reference/objectives of the Steering Committee:
 - Charged with the responsibility of developing a unified Code of Corporate Governance that will enable the Financial Reporting Council of Nigeria, among other things, to:
 - promote the highest standards of corporate governance in both private and public sectors of the Nigerian economy;
 - Promote public awareness about corporate governance principles and practices;
 - Act as the national coordinating body responsible for all matters pertaining to corporate governance in both private and public sectors of the Nigerian economy;
 - Promote sound financial reporting and accountability based on true and fair financial statements duly audited by competent independent auditors;
 - Encourage sound systems of internal control and information systems control to safeguard stakeholders' investment and assets of public interest entities (PIEs); and
 - Ensure that audit committees of PIEs keep under review the scope of audit and its cost effectiveness, the independence and objectivity of the auditors.



Terms of Reference – Technical Committee



My understanding of the terms of reference/objectives of the Technical Committee:

- To review the suspended NCCG, taking into cognisance the extensive public commentary received on the suspended Codes;
- Develop/recommend the revised Code(s); and
- Carry out all such activities as are necessary to give effect to the forgoing objectives.



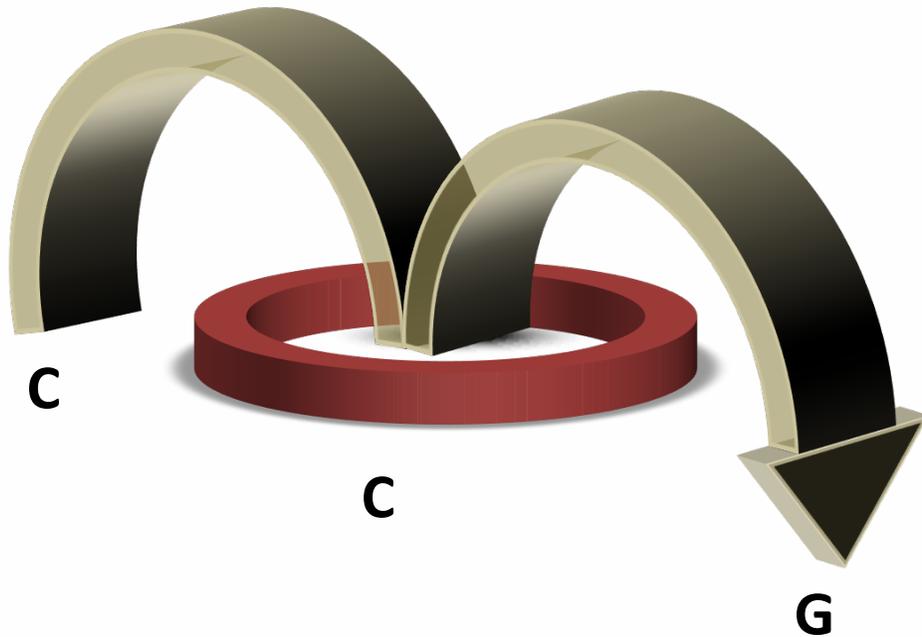
Basis of Assessment

- Our Basis of Assessing the quality of a draft Corporate Governance codes rests on three pillars:
 - Is it at the level of or in line with leading practice?
 - Does it reflect common practice?
 - Is it in line with corporate governance literature?



One

Our understanding of the Mandates/Objectives of the Technical Committee, if accurate, was not adhered to by members of the committee



- There was no mention of or reference to the suspended National Code of Corporate Governance (NCCG 2016)
- The NCCG was not cited in the Draft Nigerian Code of Corporate Governance (NCCG 2018)
- The literature listed on the “Bibliography” on page 45 of the Draft Nigerian Code of Corporate Governance (NCCG 2018) does not include the NCCG 2016
- It can be concluded from a scholarly perspective that on the basis of the evidence from the three aforementioned bullet points, nothing was taken from the NCCG 2016



Two

The “Apply and Explain” Approach to Corporate Governance was wrongly explained in the NCCG 2018 and has a far-reaching misleading effect on the application of the Code

- Although it was stated under **Section C. Para. 2** that the implementation of the Code is based on the “Apply and Explain” approach, “which assumes application of all principles, and requires entities to explain how the principles are applied” (NCCG, 2018, p. v), as well as requiring “companies to take responsibility for demonstrating how the specific activities they have undertaken best achieve the intended outcomes of the corporate governance specifications in the Principles” (NCCG, 2018, p. v), we observed that the main approach explained under **Para. 2 Page vi** and implemented in the Code was the “Apply or Explain” philosophy



The “Apply and Explain” Approach to Corporate Governance was wrongly explained in the NCCG 2018 and has a far-reaching misleading effect on the application of the Code



- First, there is no code in the world that is “Voluntary” as being interpreted in Nigeria. Nobody releases a Code in any part of the world with the intention that it should or would not be complied with.
- In actual sense, voluntary application of principles-based corporate governance codes as globally intended, whether in jurisdictions that practice “Comply or Explain,” “Apply or Explain” or “Adopt or Explain,” simply refers to the application of established corporate governance principles, provisions and practices, and, where the board finds it impracticable or unable to implement any of the provisions or recommended practices, not the principle, the board can apply a suitable alternative to achieve the intended outcome(s). The irony is that to now interpret the word “Voluntary” to mean that the board or the organisation can decide not to implement a provision or the entire Code at all, as well as not provide and explain a suitable alternative practice adopted is farther from the intent of the framers of principles-based codes worldwide.



The “Apply and Explain” Approach to Corporate Governance was wrongly explained in the NCCG 2018 and has a far-reaching misleading effect on the application of the Code

- It is important to state that even the UK that introduced the Principles-based philosophy under its “Comply or Explain” approach in 1992 does not use the word “Voluntary” anymore in its codes of corporate governance. A check on the 2008, 2010, 2012, 2014 and 2016 produced zero match for the word “Voluntary.”



The “Apply and Explain” Approach to Corporate Governance was wrongly explained in the NCCG 2018 and has a far-reaching misleading effect on the application of the Code



In addition, the Financial Reporting Council of UK in its Guidance on “What Constitute an Explanation Under ‘Comply or Explain’?” issued in February 2012 stated that “In no case did a company that failed to comply with a provision of the Code fail to provide any explanation” (**Para. 3 page 1 Introduction**). The Guidance further stated that “most instances of non-compliance relate to only one or two provisions of the Code (**Para. 4 page 1 Introduction**). In conclusion, the Guidance stated that the aim of the “Comply or Explain” principle was to ensure that, “where companies do choose to explain, the explanation is as full as is necessary to meet the expectations of shareholders (**Para. 6 page 1 Introduction**).



The “Apply and Explain” Approach to Corporate Governance was wrongly explained in the NCCG 2018 and has a far-reaching misleading effect on the application of the Code

Supporting Codes:

The UK Code of Corporate Governance 2016 states that “The Code is not a rigid set of rules. It consists of principles (main and supporting) and provisions. The Listing Rules require companies to apply the Main Principles and report to shareholders on how they have done so. The principles are the core of the Code and the way in which they are applied should be the central question for a board as it determines how it is to operate according to the Code” **(Para. 2 Page 4)**. “It is recognised that an alternative to following a provision may be justified in particular circumstances if good governance can be achieved by other means. A condition of doing so is that the reasons for it should be explained clearly and carefully to shareholders, who may wish to discuss the position with the company and whose voting intentions may be influenced as a result. In providing an explanation, the company should aim to illustrate how its actual practices are consistent with the principle to which the particular provision relates, contribute

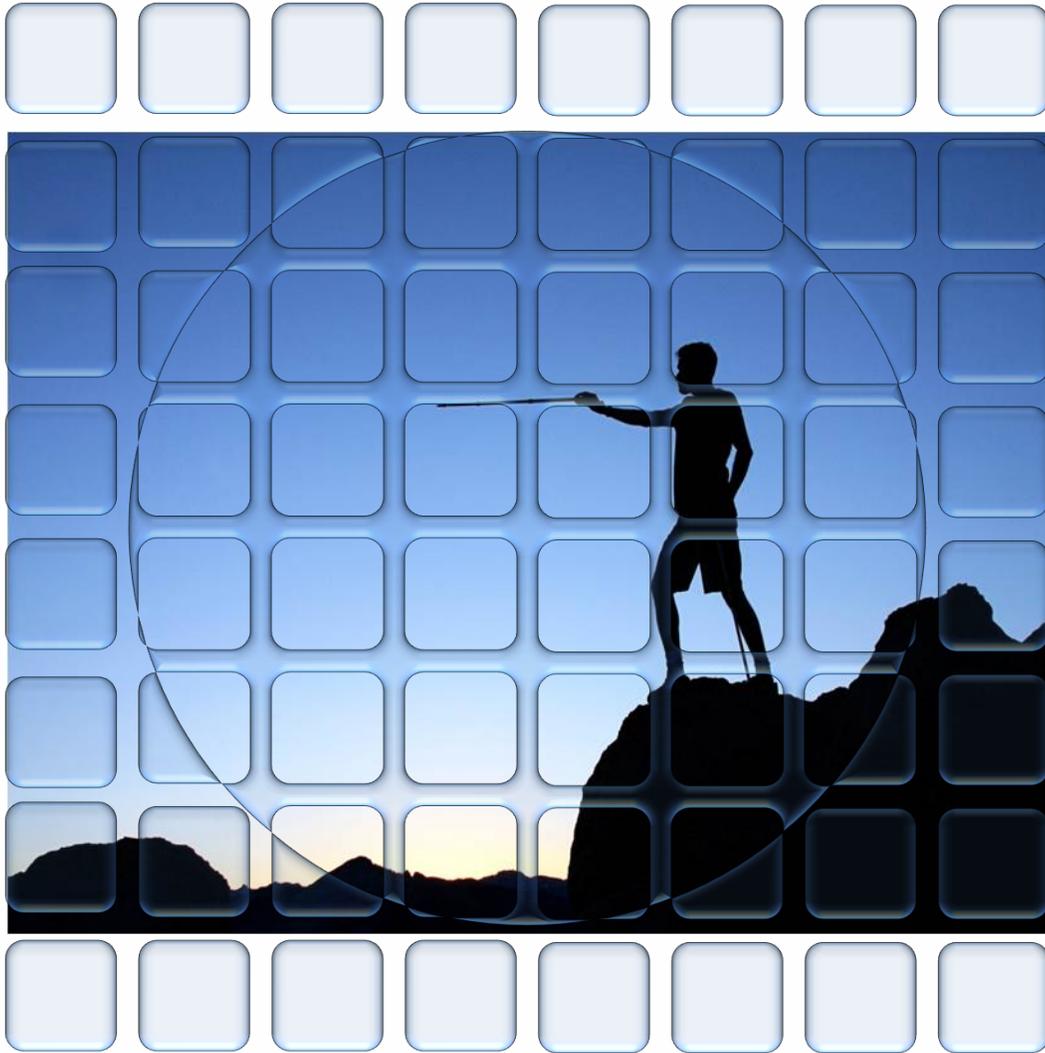


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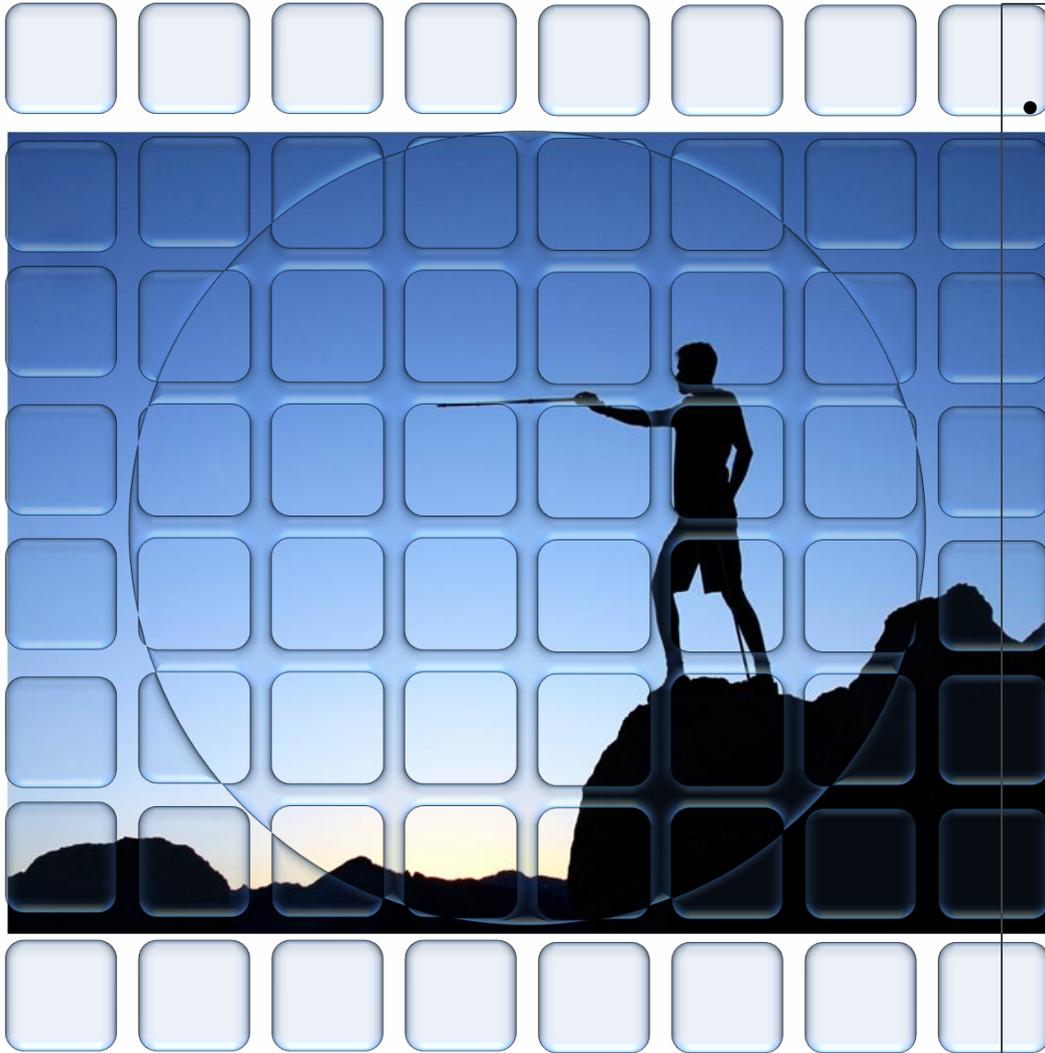
to good governance and promote delivery of business objectives. It should set out the background, provide a clear rationale for the action it is taking, and describe any mitigating actions taken to address any additional risk and maintain conformity with the relevant principle. Where deviation from a particular provision is intended to be limited in time, the explanation should indicate when the company expects to conform with the provision” (Para. 3 Page 4).





- King IV (2016) adopts the “Apply and Explain” philosophy and states that “The legal status of King IV, as with its predecessors, is that of a set of voluntary principles and leading practices” (**Para. 1 Page 35**).
- The Malaysian Code on Corporate Governance 2017 (MCCG 2017) adopts the “Apply or Explain” approach and states that the “boards should apply the practices by taking into account the environment that their companies operate in, size and complexity, and the nature





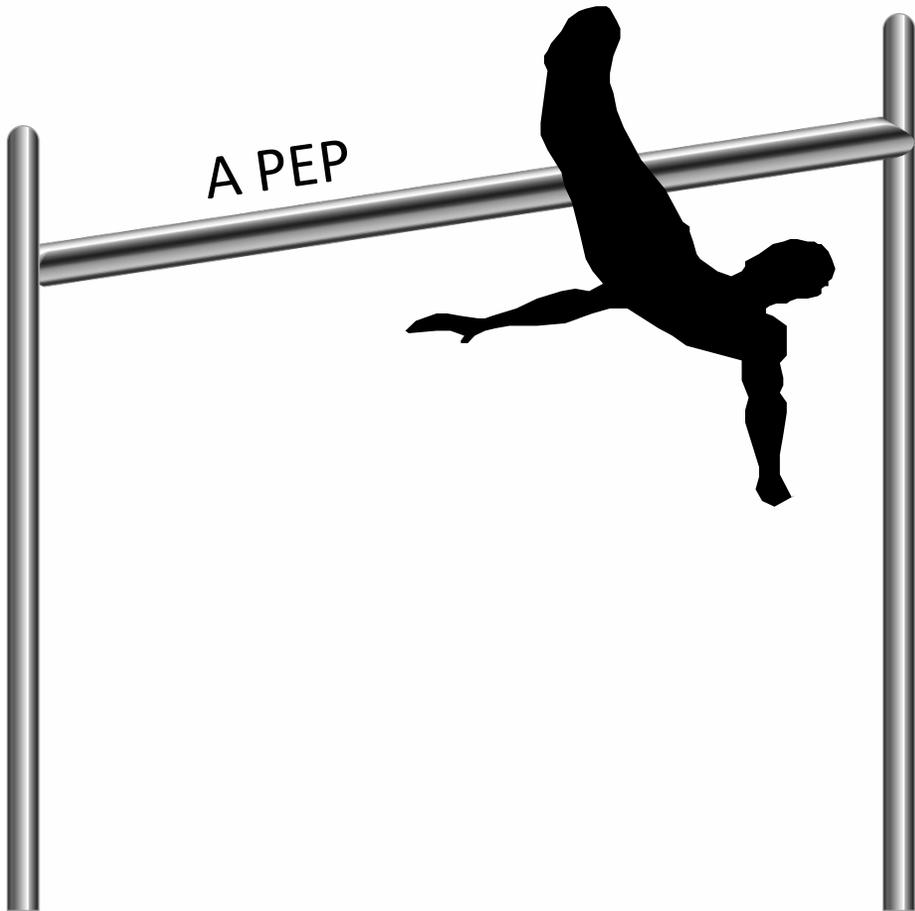
• The Malaysian Code on Corporate Governance 2017 (MCCG 2017) adopts the “Apply or Explain” approach and states that the “boards should apply the practices by taking into account the environment that their companies operate in, size and complexity, and the nature of risks and challenges faced” (**Para. 5.3 Page 8**). However, “If the board finds that it is unable to implement any of the MCCG practices, the board should apply a suitable alternative practice to meet the Intended Outcome. For Large Companies, the board is also expected to disclose the measures they have taken or intend to take to enable them to adopt the MCCG Practice(s), and the timeframe required” (**Para. 5.4 Page 8**). Finally, “The Guidance in the MCCG explains how the practices may be applied to achieve the Intended Outcome. The board should do its best to adhere to the Guidance when implementing the MCCG practices” (**Para. 5.5 Page 8**)





- The Egyptian Corporate governance Code 2016 adopts the “Comply or Explain” principle and states that “As a rule, and without prejudice to the mandatory compliance with laws and regulations, a company should typically seek to apply all the relevant principles outlined in this Code. If it fails to do so, for whatever reason, the company must provide an objective and justifiable explanation, in application of the “Comply or Explain” principle. Every company is required to consider all the principles outlined in the present Code, specify the principles it complies with and those it deviates from, the justification of non-compliance, and its future plan for implementing them. This report is to be posted on the Company’s website and be published in its annual report for shareholders (**Para. 1.6**).





- The National Code of Corporate Governance for Mauritius 2016 (Mauritius NCCG) adopts the “Apply and Explain” corporate governance approach and states that “Rather than being a rigid set of rules, the Code comprises eight principles on just two pages. The principles form the core of the Code. Every Board of directors should decide how to apply each principle (**Para. 5 Page 7**). In addition, “The Board should focus on the annual report’s explanation of how an entity has applied the principles. Guidance is provided to prompt the producers of the annual report to consider responses to the following questions” (**Para. 6 Page 7**):





Three

- **The Authority of the Code**
- **Para 1 Section A. Page iv** of the NCCG 2018 states that “The Nigerian Code of Corporate Governance 2018 is issued pursuant to this authority and in line with international leading governance practices, learning points garnered from the experiences of other jurisdictions and the feedback received from stakeholders during consultative sessions.”
- Whilst the issue of authority is not in question, most of the provisions of this Code do not reflect international leading (nor common) governance practices, learning points garnered from other experience of other jurisdictions. The Code as written does not have the capacity to achieve leading practice status, such as achieved by the King Code of South Africa (1994, 2002, 2009, 2016). Examples of its extensive shortcomings are highlighted succeeding bullet points





Three

- **Board Composition:**
 - **The NCCG 2018** under **Para. 2.3b** states that “appropriate mix of Executive, Non-executive and Independent Non-executive members such that majority of the Board are Non-executive Directors. **It is advisable that most of the NEDs are independent.**” This is neither in line with leading practice, common practice nor corporate governance literature
 - Independent directors concept is the safeguard mechanism in a unitary board system
 - **The Malaysian Code (MCCG 2017)** states that “At least half the board comprises independent directors. For large companies, the board should comprise a majority of independent directors” (**Para. 4.1**)





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- **Board Composition:**
- French Code 2016 states that “ The INEDs should account for half the members of the Board” (**Para. 8.2**)
- **The NCCG 2018** under **Para. 2.3b** states that “appropriate mix of Executive, Non-executive and Independent Non-executive members such that majority of the Board are Non-executive Directors. **It is advisable that most of the NEDs are independent.**” This is neither in line with leading practice, common practice nor corporate governance literature
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- Ghana Corporate governance guidelines on best practices 2009 states that “ The board should include a balance of EDs and NEDs with the complement of independent directors being at least one-third of the total membership of the board and in any event not less than two” (**Para. 21**). The Ghana Code also states that “No specific number are prescribed with regard to membership, however, a board of between 8 and 16 members is considered ideal” (**Para. 6**)



Three

Shadow Director:

The NCCG 2018 under **Para. 2.10** states that “A person or group of individuals who is not a serving Director of the Company should not exercise any influence or dominance over the Board and/or Management. Such a person or group of individuals would be deemed a shadow director as defined by extant laws.”

What are the safeguards to prevent this from happening and if it does happen what are the consequences? It is not enough to state this without safeguards





Three

- **Chairman being NED:**
 - The Chairman of the Board should be a NED and not be involved in the day-to-day operations of the Company, which should be the primary responsibility of the MD/CEO and the management team.
 - **Kenya Draft Code 2014** states that “The chairperson of a public listed company should be an independent director **(Recommendation. 1.3.4)**”
 - **Mauritius NCCG** states that “All Boards should have a Chairperson who may be independent” **(Para. 3 Page 17)**
 - **The UK Code 2016** states that “The chairman should on appointment meet the independence criteria set out in B.1.1 of Page 10 of the Code” **(A.3.1. Page 8)**
- **King IV 2016** states that “The governing body should elect an independent non-executive member as chair to lead the governing body in the objective and effective discharge of its governance role and responsibilities **(Para. 31 Page 53)**”





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- **Appointment of Directors:**
- **The NCCG 2018 states that** “A written, clearly defined, rigorous, formal and transparent procedure serves as a guide for the selection of Directors to ensure the appointment of high quality individuals to the Board” (**Principle 12 Page 18**)
- The choice of language used here (“serves as a guide”) is not a leading practice nor a common practice language
- **The UK Code of CG 2016** states that “There should be a formal, rigorous and transparent procedure for the appointment of new directors the board (Para. B.2.)
- **Principle 10 Page 58 of King IV** states that “The governing body should ensure that the appointment of, and delegation to, management contribute to role clarity and the effective exercise of authority and responsibilities”





Three

- **Re-election of Directors:**
- **The UK Code of CG 2016** states that “All directors should be submitted for re-election at regular intervals, subject to continued satisfactory performance” (**Principle B.7**)
- **The UK Code of CG 2016** states that “All directors should be subject to election by shareholders at the AGM after their appointment and to re-election thereafter at intervals of no more than three years (**Para B.7.1**)
- **The UK Code of CG 2016** states that “The board should set out to shareholders in the papers accompanying a resolution to elect a NED or INED why they believe an individual should be elected. The chairman should confirm to shareholders when proposing re-election that, following formal performance evaluation, the individual’s performance continues to be effective and to demonstrate commitment to the role” (**Para. B.7.1**)





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ACADEMY

QUESTIONS



Thank you Thank you Thank you

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