

Understanding concepts of Governance

Governance

- refers to a process whereby elements in society wield power, authority and influence and enact policies and decisions concerning public life and social uplift.
- means the process of decision-making and the process by which decisions are implemented (or not implemented) through the exercise of power or authority by leaders of the country and/or organization.

Corporate Governance

- system of rules, practices and processes by which business corporations are directed and controlled.
- Corporate governance is of paramount importance to a company and is almost as important as its primary business plan. It enhances a company's image in the public eye as self policing company that is responsible and worthy of shareholder and debtholder capital. It dictates the shared philosophy, practices and culture of an organization and its employees. A corporation without a system of corporate governance is often regarded as a body without a soul or conscience.

Characteristic of Good Corporate Governance

The major characteristic of good governance as shown above are as follows:

1. **Participation.** It could be either direct or through legitimate institutions or representatives. It needs to be informed and organized. This means freedom of association and expression on one hand and an organization civil society on the other hand.
2. **Rule of law.** Good governance requires fair legal frameworks that are enforced impartially and requires full protection of human rights.
3. **Transparency.** Decisions taken and their enforcement are done in a manner that follows rules and regulations. Information is freely available and directly accessible to those who will be affected by such decisions and their enforcement.
4. **Responsiveness.** Good governance requires that institutions and processes try to serve needs of all stakeholders within the reasonable timeframe.
5. **Consensus Oriented** Mediation of the different interest in society is required. It also requires broad and long-term perspective on what is needed for sustainable human development and on how to achieve the goals of such development.
6. **Equity & Inclusiveness.** Ensures that all its members feel that they have stake in it and have opportunities to improve or maintain their well-being.
7. **Effectiveness & Efficiency** The processes and institutions produce results that meets the need of the society while making the best use of resources at its disposal.
8. **Accountability.** The key requirement of a good governance. Organization or institution is accountable to those who will be affected by its decisions or actions. Accountability can not be enforced without transparency and rule of law.

Relevance of Good Governance to SMEs and Publicly listed companies

Small Medium Enterprise

- are businesses that maintain revenues, assets or a number of employees below certain threshold.
- Each country has its own definition of what constitutes a SMEs.
- Businesses with not more than 100M assets and not more than 199 employees.
- Example: Markina shoemakers

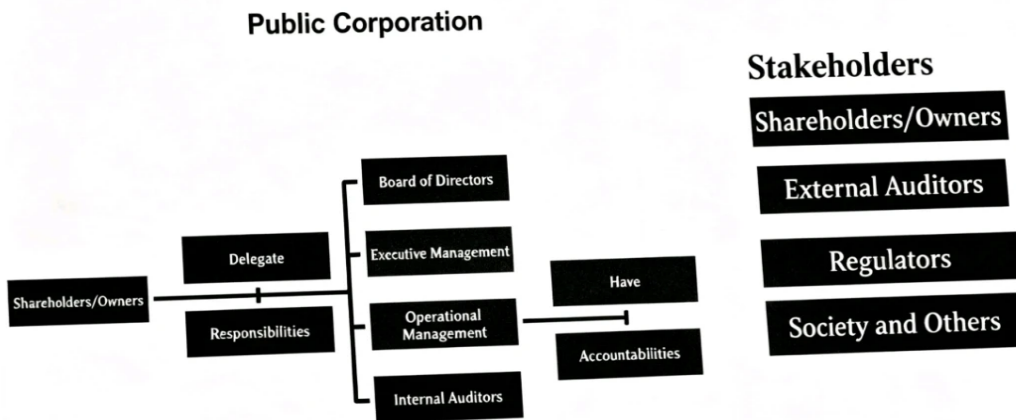
Publicly-listed Companies

- A company that has held an initial public offering and whose shares are traded on a stock exchange in the over-the-counter market.
- Example: ABS CBN, PHINMA Corp, Ayala Corp, etc.

Regardless of the size and type, the issue on good governance has become increasingly important. Note that there is no single universal formula for a good corporate governance. All organization are encouraged to give appropriate attention to the principles and adopt approaches that are tailored to the specific needs of the organization at a given point in time. The essence of any good corporate governance system is to allow the board and management the freedom to drive their organization forward and exercise it within the framework of effective accountability.

Relationship of Shareholders and Other Stakeholders

Below shows the framework of Corporate Governance:



There is a clear-cut distinction between ownership and professional management of the company. And all stakeholders are informed about the day to day operations through various reports and data.

LO3: Responsibilities of Member of the Corporate Governance

Party	Overview of Responsibilities
Shareholders	- Provide effective oversight through election of board members - Approval of major initiatives such as buying and selling stocks, annual report on management compensation
Board of Directors	- Overall Operations - Establishing organization mission, vision and ethical standards. - Delegating an appropriate level of authority to management - Demonstrating leadership - Assuming responsibility for the business relationship with COE including his or her appointment, succession, performance, remuneration and dismissal. - Overseeing aspects of the employment of the management team. - Recommending auditors and new directors to shareholders - Ensuring effective communication with shareholders and other stakeholders. - Crisis Management - Appointment of the CEO and corporate secretary - Performance - Ensuring long term viability and enhancing financial position - Formulate and oversee implementation of corporate strategy

	• Approving the plan, budget and corporate policies • Agreeing Key performance Indicators (KPI) • Monitoring/ assessing assessment, performance of the organization, the board itself, management and major projects. • Overseeing the risk management framework and monitoring business risk • Monitoring development in the industry and the operating environment • Oversight of and the organization, including its control and accountability systems. • Approving and monitoring the progress of major capital expenditure, capital management and acquisition and divestitures. 3) Compliance • Understanding and protecting the organization's financial position • Requiring and monitoring legal and regulatory compliance • Approving annual financial reports, annual reports and other public documents/sensitive reports. • Ensuring effective system of internal controls.
Independent Directors	• To understand that his role is not to act as auditor, nor as a member of management team. • To understand the organizations, its business, its operating environment and financial position • To apply expertise and skills in organization's best interest • To assist management to keep performance objectives at the top of agenda • To respect the collective, cabinet nature of the board's decision • To prepare for and attend board meeting
	• To seek information on a timely basis to ensure that he is in position to contribute to the discussion when a matter comes before the board or alert the chairman in advance to the need of further information • To ask appropriate question relative to operations.
Management	Board Role: Manage the organization effectively, provide accurate and timely reports to the shareholders and other stakeholders • Recommend the strategic direction and translate the strategic plan into the operation of the business • To run the business • Assume day to day responsibility for the organization conformance with relevant laws and regulations and its compliance framework. • Develop, implement and manage the organization risk management and internal control framework • Develop, implement and update policies and procedures • Be alert to relevant trend in the industry • Provide information to the board • Act as conduit between board and organization • Develop financial and other reports to meet public, stakeholders and regulatory requirement.
Audit Committee of Board of Directors	Broad Role: provide oversight of the internal and external audit function and the process of preparing annual financial statement a well as public reports on internal control. • Selecting the external audit firm • Approving any non-audit work performed by the audit firm • Selecting or approving of Chief Audit Executive • Reviewing and approving the scope and budget of internal audit function

	Discussing audit findings with internal auditor and external auditor and advising the board
Regulators A. Board of Accountancy B. Securities and Exchange Commission	Board Role: Set accounting and auditing standards dictating underlying financial reporting and auditing concepts; set of expectation of audit quality and accounting quality. - Conducting CPA Licensure Board Examinations - Approving accounting principles - Approving auditing standards - Interpreting previously issued standards implementing quality control processes to ensure audit quality. - Educating members on audit and accounting requirements Board Role: Ensure the accuracy, timeliness and fairness of public reporting of financial and other information for public companies. - Reviewing filing with the SEC - Interacting with FRSC in setting accounting standards - Specifying independence standards required of auditors that report on public financial statements - Identify corporate frauds, investigative causes, and suggest remedial actions.
External Auditors	Board Role: Performs audit of company financial statements to ensure that the statements are free of material misstatements including misstatements that maybe due to fraud. - Audit of public company financial statements - Audit of nonpublic company financial statements - Other services such as tax or consulting
Internal Auditors	Board Role: Perform audit of companies for compliance with company policies and laws, audit to
	evaluate efficiency of operations, and periodic evaluation and test of controls. - Reporting results and analysis to management and audit committee - Evaluating internal control

B.MAIN LESSON

1) Activity 2: Content Notes (13 mins)

LO1: Understanding Code of Governance and need for Publicly listed Companies

- What is the name of the code?
Code of Corporate Governance
- When It was approved?
SEC Code of Governance was released on November 10, 2016 during the 3rd Annual SEC PSE Corporate Governance Forum.
- What is the purpose of its released?
To raise the corporate governance standards of Philippine corporations to a level at par with regional and global counter parts.
- How's the arrangement of the Code?
It is arranged as to 1.) Principle, 2.) Recommendation, 3.) Explanation
- What companies are covered by the Code?
All registered companies and branches or subsidiaries of foreign corporations operating in the Philippines that
 - a) Sell equity and/ or debt securities to the public that are required to be registered with the commission
 - b) Have assets in excess of 50M and at least 200 stockholders who own at least 100 shares of equity securities
 - c) Whose equity are listed on an Exchange
 - d) Grantees of secondary license from the commission
- What is Exchange?
An organized marketplace or facility that brings together buyer and seller, and execute trade of securities and/or commodities. Example is Philippine Stock Exchange.

➤ What are publicly-listed companies?

Those companies whose securities are listed and traded at Exchange. Examples are ABS CBN, PHINMA Corp., Ayala Corp.

L02: Understanding the Three Aspects of the Code and its feature, "comply or complain" approach

The Code of Corporate Governance is arranged as follows:

- 1. Principles** – can be considered to be a high-level statements of corporate governance good practices and are applicable to all companies.
- 2. Recommendations** – objective criteria that are intended to identify the specific features of corporate practice that are recommended for companies operating according to the Code. Alternatives to the recommendation may be justified in a particular circumstance if good governance can be achieved by other means.
- 3. Explanations** – strive to provide companies with additional information on the recommended best practice

Comply or Complain approach combines the voluntary compliance with mandatory disclosure. Companies do have to comply with the code, but they must state in their annual corporate governance reports whether they comply with the Code Provisions, identify any areas of non-compliance, and explain the reasons for non-compliance.

L03. 16 Principles of Code of Corporate Governance

The Code of Corporate Governance have 16 principles that are distributed among 5 main sections:

- Board's Governance Responsibilities – Principle 1-7
- Disclosure and Transparency – Principle 8 -11
- Internal Control and Risk Management Framework – Principle 12
- Cultivating a Synergic Relationship with Stakeholders – Principle 13
- Duties to Stakeholders – Principle 14 – 16

SECTION	PRINCIPLE	Recommendation	Explanation
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Board's Governance Responsibilities (Principle 1-7)	Principle 1 – Establishing a competent board A company should be headed by a competent, working board to foster the long-term success of the corporation, and to sustain its competitiveness and profitability in a manner consistent with its corporate objectives and the long-term best interest of its shareholders and other stockholders.	1.1 Board should always ensure that it has appropriate mix of expertise relevant to company's industry/sector	1.1 Competence enables company to properly perform its task of overseeing management and governance of the corporation, formulating vision, mission, strategic objectives, policies and procedures.	1.6 should have a Compliance Officer who is a.) Should have the rank of Senior Vice President or an equivalent position with adequate stature and authority; b.) not member of BOD; c.) annually attend training on corporate governance	board meeting except for a justifiable cause, oversees drafting of by-laws, perform other duties provided by the SEC. 1.6 Ensures proper onboarding of new directors, monitors, review, evaluate compliance with this Code and other regulations, reports violation and recommend appropriate disciplinary actions, ensures integrity of all documents, appears before SEC when summoned in relation to compliance of the Code, ensures attendance of board and key officers in relevant trainings, collaborates with other department, identifies possible areas of compliance.
		1.2 Should composed of majority of non-executive directors who possess the necessary qualifications to effectively participate and help secure objective, independent judgment on corporate affairs and to substantiate proper checks and balances.	1.2 Right combination ensures that no director or small group of directors can dominate the decision-making process.		
		1.3 Should have a policy on the training of its directors, including an orientation program for first-time directors and relevant annual continuing training for all directors.	1.3 Orientation program for the first-time directors aim to promote effective board performance and continuing qualification of the directors in carrying out their duties and responsibilities.	Principle 2 – Establishing Clear Roles and Responsibilities of the Board The fiduciary roles, responsibilities and accountabilities of the Board as provided under the law, the company's articles and by-laws, and other legal pronouncements and guidelines should be clearly made known to all directors as well as to shareholders and other	2.1 The Board members should act on a fully informed basis, in good faith, with due diligence and care, and in the best interest of the company and all shareholders. 2.2 should oversee the development of and approve the company's business objectives and strategy, and monitor their implementation, in order to sustain the company's long-term viability and strength. 2.3 should be headed by a competent and qualified Chairperson.
		1.4 should have a policy on board diversity.	1.4 This is a move to avoid groupthink and ensure that optimal decision-making is achieved.		
		1.5 should have a Corporate Secretary, who is: a.) separate individual from compliance officer; b.) not member of BOD; c.) annually attend training on corporate governance	1.5 Assist the board and board committees in the conduct of their meetings, safekeeps and preserves integrity of minutes of meeting, keeps abreast of relevant laws and regulations, works fairly and objectively with the board, advises on the establishment of board committee, informs members of the board of meeting agenda 5 days in advance, attends all		2.1 Fiduciary duty of board members are duty of care and duty of loyalty. 2.2 Sound strategic policies and objectives translate to company's proper identification and prioritization of its goals and guidance on how best to achieve them. 2.3 Chairman makes certain that the meeting agenda focuses on strategic matters, guarantees accurate, timely, relevant, insightful information., facilitate
stakeholders		2.4 should be responsible for ensuring and adopting an effective succession planning program for directors, key officers and management.	2.4 The goal of succession plan is he transfer of company leadership to highly competent and qualified individuals and a good succession plan is linked to documented roles and responsibilities for each position.	Principle 3 – Establishing Board Committees Board committees should be set up to the extent possible to support the effective performance of the Board's functions, particularly with respect to audit, risk management, related party transactions, and other key corporate governance concerns, such as nomination and remuneration. The composition, functions and responsibilities of all committees established should be contained in a publicly available Committee Charter.	2.10 should oversee that an appropriate internal control system is in place. 2.11 should oversee that a sound enterprise risk management (ERM) framework is in place. 2.12 should have a Board Charter that formalizes and clearly states its roles, responsibilities and accountabilities in carrying out its fiduciary duties.
		2.5 should align the remuneration of key officers and board members with the long-term interests of the company.	2.5 To attract and retain the services of qualified and competent individuals.		
		2.6 should have a formal and transparent board nomination and election policy.	2.6 It should encourage shareholders participation		
		2.7 should have the overall responsibility in ensuring that there is a group-wide policy and system governing related party transactions (RPTs) and other unusual or infrequently occurring transactions.			
		2.8 should be primarily responsible for approving the selection and assessing the performance of the Management.			
		2.9 should establish an effective performance management framework that will ensure that the Management, including the Chief Executive Officer, and personnel's performance is at par with the standards set by the Board and Senior Management			

	Principle 4 – Fostering Commitment To show full commitment to the company, the directors should devote the time and attention necessary to properly and effectively perform their duties and responsibilities, including sufficient time to be familiar with the corporation's business	4.1 The directors should attend and actively participate in all meetings of the Board, Committees, and Shareholders in person or through tele/videoconferencing conducted in accordance with the rules and regulations of the Commission. 4.2 non-executive directors of the Board should concurrently serve as directors to a maximum of five publicly listed companies. 4.3 A director should notify the Board where he/she is an incumbent director before accepting a directorship in another company.	*
	Principle 5 – Reinforcing Board Independence The board should endeavor to exercise an objective and independent judgment on all corporate affairs.	5.1 The Board should have at least three independent directors, or such number as to constitute at least one-third of the members of the Board, whichever is higher. 5.2 should ensure that its independent directors possess the necessary qualifications and none of the disqualifications for an independent director to hold the position. 5.3 The Board's independent directors should serve for a maximum cumulative term of nine years. 5.4 The positions of Chairman of the Board and Chief Executive	*

		Officer should be held by separate individuals and each should have clearly defined responsibilities. 5.5 The Board should designate a lead director among the independent directors if the Chairman of the Board is not independent. 5.6 A director with a material interest in any transaction affecting the corporation should abstain from taking part in the deliberations for the same. 5.7 The non-executive directors (NEDs) should have separate periodic meetings with the external auditor and heads of the internal audit, compliance and risk functions, without any executive directors' present to ensure that proper checks and balances are in place within the corporation.	
	Principle 6 – Assessing Board Performance The best measure of the Board's effectiveness is through an assessment process. The Board should regularly carry out evaluations to appraise its performance as a	6.1 The Board should conduct an annual self-assessment of its performance, including the performance of the Chairman, individual members and committees. Every three years, the assessment should be supported by an external facilitator. 6.2 The Board should have in place a system that provides, at the minimum, criteria and process to	*

	body, and assess whether it possesses the right mix of backgrounds and competencies	determine the performance of the Board, the individual directors, committees and such system should allow for a feedback mechanism from the shareholders.	
	Principle 7 – Strengthening Board Ethics Members of the Board are duty-bound to apply high ethical standards, taking into account the interests of all stakeholders.	7.1 The Board should adopt a Code of Business Conduct and Ethics. 7.2 The Board should ensure the proper and efficient implementation and monitoring of compliance with the Code of Business Conduct and Ethics and internal policies.	*
DISCLOSURE AND TRANSPARENCY (Principle 8-11)	Principle 8 – Enhancing Company Disclosure Policies and Procedures	8.1 The Board should establish corporate disclosures and policies. 8.2 The Company should have policy requiring all directors and officers to disclose/report any dealings in the company's shares within 3 business days. 8.3 The board should fully disclose all relevant and material information on individual board members and key executives. 8.4 Company should provide clear disclosure of its policies and procedures for setting board and executive remuneration as well as the level and mix of the same in the Annual Corporate Governance Report.	

		8.5 The company should disclose its policies governing Related Party Transaction and other unusual or infrequently occurring transactions in their manual on corporate governance. 8.6 The company should make full, fair, accurate and timely disclosure to the public of every material fact or event that occurs. 8.7 The company's corporate governance policies, programs and procedures should be contained in its Manual on Corporate Governance.	
	Principle 9 – Strengthening the External Auditor's Independence and Improving Audit Quality	9.1 The Audit Committee should have robust process for approving and recommending the appointment, reappointment, removal, and the fees of external auditor. 9.2 The Charter should include Audit Committee's responsibility on assessing the integrity and independence of external auditors and exercising effective oversight to review and monitor their independence and objectivity taking in consideration the Philippine professional and regulatory requirements. 9.3 The company should disclose the nature of non-audit services performed by its external auditor in the Annual	

Report to deal with the potential conflict of interest.

Note: For a complete copy of this code follow the link, http://www.sec.gov.ph/wp-content/uploads/2016/12/2016_memo_circular_no.19.pdf.

SECTION	PRINCIPLE	RECOMMENDATION	EXPLANATION
	Principle 10 – Increasing Focus on Non-Financial and Sustainability Reporting	10.1 The board should have clear and focused policy on the disclosure of non-financial information, with emphasis on the management of economic, environmental, social and governance (EESG) issues of its business.	Disclosure is required to respond to sustainability challenges to determine their long-term viability and competitiveness
	Principle 11 – Promoting Comprehensive and Cost-Efficient access to relevant information	11.1 The company should include media and analyst' briefings as channels of communication to ensure the timely and accurate dissemination of public, material and relevant information to its shareholders and other investors.	11.1 Communication channels can provide timely and up-to-date information relevant to investor's decision-making, as well as to other interested stakeholders.
Internal Control System and Risk Management Framework	Principle 12 – Strengthening the Internal Control System and Enterprise Risk Management Framework	12.1 The company should have adequate and effective internal control system and enterprise risk management framework in the conduct of its business taking into account its size, risk profile and complexity of operations. 12.2 Company should have in place an independent internal audit function that provides independent and objective assurance, and consulting services designed to add value and improve the company's operations.	12.1 Help sustain safe and sound operation as well as implement management policies to attain corporate goals. 12.2 Essential to monitor and guide the implementation of company's policies. Systematic and disciplined evaluation approach improves effectiveness of the company's governance, risk management and control functions.

		12.3 Subject to company's size, risk profile and complexity of operations, it should have a qualified Certified Audit Executive appointed by the board. 12.4 Subject to company's size, risk profile and complexity of operations, the company should have separate risk management function to identify, assess and monitor key risk exposure.	12.3 CAE directly reports functionality to the Audit Committee and administratively to CEO. 12.4 Risk management function define risk management strategy, identify and analyze risk, evaluate and categorize, establish risk register, develop risk mitigation, communicate and report significant risk monitor and evaluate the effectiveness of organization's risk management risk process.
		12.5 The Company should have Risk Management System who is the ultimate champion of Enterprise Risk Management.	12.5 CRO supervises the entire ERM process and spearheads the development, implementation, maintenance and continuous improvement, communicate top risk to Board Risk Oversight Committee, collaborates with CEO in updating and making recommendation, suggest ERM policies, provides insight on risk management and measures
CULTIVATING SYNERGIC RELATIONSHIP WITH SHAREHOLDERS	Principle 13 – Promoting Shareholder Rights	13.1 The board should ensure that basic shareholder rights are disclosed in the Manual of Corporate Governance and on company's website. 13.2 Board should encourage active shareholder participation by sending Notice of Annual and Special Shareholders' Meeting at least 28 days before the meeting. 13.3 Board should encourage active shareholder participation	13.1 It is the board responsibility to adopt a policy informing the shareholder of their rights. 13.2 IT allows shareholders to plan their participation in meeting. 13.3 Substantial number of votes against proposal made by

		by making results of the votes taken during the most recent Annual or Special Shareholder's meeting publicly available in the next working day. 13.4 The board should make available, at the option of a shareholder, an alternative dispute mechanism to resolve intra-corporate disputes in amicable and effective manner. 13.5 Board should establish an Investor Relations Officer to ensure constant engagement with its shareholders. IRO should be present at every stockholder's meeting.	management may make analysis of reasons and consider having dialogue with its shareholders. 13.4 Ensures suitable remedies for the infringement of shareholder's rights and prevents excessive litigation. 13.5 Ensures that all information regarding the activities of a company are properly and timely communicated to shareholders.
DUTIES TO STAKEHOLDERS (Principle 14-16)	Principle 14 – Respecting Rights of Stakeholders and effective redress for Violation of Stakeholder's Rights	14.1 The Board should identify the various stakeholders and promote cooperation between them and the company in creating wealth, growth and sustainability. 14.2 The Board should establish clear policies and program to provide mechanism on the fair treatment and protection of stakeholders. 14.3 The Board should adopt a transparent framework and process that allow stakeholders to communicate with the company and to obtain redress for the violation of their rights.	14.1 Due consideration is given to those who have interest in the company and are directly affected by its operations. 14.2 The company's code of conduct ideally include provision on the company's policies and procedures on dealing with various stockholders. 14.3 Company's stakeholders plays important role in its growth and long-term viability hence it is crucial to maintain open and easy communication with its stakeholders.
	Principle 15 – Encouraging Employee participation.	15.1 The Board should establish policies, programs and procedures that encourage employee to actively participate	15.1 Policies and programs on 1.) health, safety and welfare; 2.) training and development; 3.) rewards/ compensation

		in the realization of company's goals and its governance. 15.2 The Board should set the tone and make stand against corrupt practices by adopting anti-corruption policy and program in its Code of Conduct. 15.3 The Board should establish a suitable framework for whistleblowing that allows employees to freely communicate their concerns illegal practices, without fear of retaliation.	encourages employees to perform better and motivates them to take a more dynamic role. 15.2 endeavors to mitigate corrupt practices such as but not limited to bribery, fraud, extortion and the like. 15.3 Sets up the procedures and safe-harbors for complaints of employees, either personally or through their representative bodies, concerning illegal and unethical behavior.
	Principle 16 – Encouraging Sustainability and Social Responsibility	16.1 The company should recognize and place an importance on the interdependence between business and society, and promote mutually beneficial relationship that allows the company to grow its business, while contributing to the advancement of the society where it operates.	16.1 Sustainable developments mean that the company not only complies with existing regulations, but also voluntarily employs value chain processes that takes into consideration economic, environmental, social and governance issues and concerns.