CORPORATE GOVERNANCE

Nine-year cap on independent directors to kick in from 2022

Definition of ‘independence’ tightened; IDs must make up at least one-third of listed boards

By Angela Tan
angela@spf.com.sg

SOME 42.2 per cent of companies listed in Singapore have at least one independent director (ID) who has been on the board for over nine years – but they will now have to fix that by January 1, 2022. All companies will also have to ensure that IDs make up one-third of their board seats.

This comes after the Monetary Authority of Singapore (MAS) on Monday made the nine-year threshold for IDs a hard limit written into the Singapore Exchange (SGX) Listing Rules. Beyond nine years, the appointment of the ID will be subject to a two-tier vote by all shareholders excluding directors, CEO and associates. If the ID is not voted in, he or she can continue to serve on the board as a non-independent director.

The nine-year cap on IDs is already practised among the local banks since 2010.

The extension of the practice to other listed companies follows a proposal by the Corporate Governance Council (CGC) in January this year to enforce the “nine-year rule” after it acknowledged that an ID who had served nine years might have had his independence compromised, given the familiarity with management, and can no longer be regarded as independent.

To date, the director with the longest tenure, before he stepped down in January this year, had been on the board for some 55 years. Before that, the record used to be 59 years, according to to Lawrence Loh, director at the Centre for Governance, Institutions and Organisations (CGIO) as well as deputy head and associate professor of Strategy and Policy at NUS Business School.

Sharing the results of the latest Singapore Governance and Transparency Index (SGTI), Prof Loh, who is the principal investigator of the study, told The Business Times that some 278 companies out of its database of 659 companies have at least one ID who has served for more than nine years.

“In other words, 42.2 per cent of companies have at least one ID who served more than 9 years. On the flip side, 57.8 per cent have all IDs with 9 years or less in tenure,” the professor said.

The SGTI 2018 results showed that companies need to gear up especially in making concerted efforts to induct IDs onto boards, he said.

“There is still quite some way to go as the number of IDs is on the high side for those who serve more than 9 years. Also, on a broader level, companies should manage their overall director tenures to create more space for IDs to come in,” Prof Loh added.

According to the study, whether a chairman is independent or non-independent also affects the proportion of independent directors.

“Companies with independent chairmen have, on average, 54.6 per cent independent directors on the board whereas those with non-independent chairmen have 51.6 per cent,” Prof Loh added.

MAS also accepted the CGC’s other recommendations to strengthen board quality, and issued the revised Code of Corporate Governance (Code), which has been significantly simplified. It now includes a more stringent definition of director independence by lowering the shareholding threshold to determine a director’s independence to 5 per cent from 10 per cent.

Ong Chong Tee, MAS deputy managing director (Financial Supervision), said: “The revised Code is more concise and less prescriptive, and is designed to encourage more thoughtful application. It will help spur better corporate governance practices among companies to sustain long-term business performance.”

Mr Ong said MAS, as the statutory regulator, deliberately calibrated rules like having more stringent CG standards for banks due to their potential systemic impact.

“Tighter across-the-board regulations could impose additional costs on all listed companies, and these costs must be weighed against the benefits,” he said.

On concerns that some of the principles in the Code are subject to interpretation and gaming, Mr Ong said the MAS has accepted the Council’s recommendation to set up a standing Corporate Governance Advisory Committee by the end of this year to monitor CG developments on a regular basis.

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Key recommendations to enhance CG

EFFECTIVE AND FUTURE-READY BOARDS
Aim: To have well-rounded and competent boards with diverse perspectives
- Rationalise tests of independence
- Reduce shareholding threshold from 10% to 5%
- 9-year rule for independent directors (IDs): Two-tier shareholders’ vote by (i) all shareholders; and (ii) all shareholders excluding directors/CEO (and associates)*
- At least one-third of board to comprise IDs*
- Majority of board to comprise IDs, where Chairman is not independent
- Majority of board to comprise non-executive directors^*
- Disclose board diversity policy and progress made^*

ENGAGED STAKEHOLDERS
Aim: For an inclusive approach beyond shareholders
- Consider and balance needs and interests of material stakeholders^*

TRANSPARENT REMUNERATION PRACTICES
Aim: To align remuneration to long-term objectives and performance
- Disclose relationship between remuneration and value-creation
- Disclose remuneration of employees who are substantial shareholders or their immediate family members^*

SUPPORTIVE ECOSYSTEM
Aim: To have advocacy initiatives to support companies
- Establish an industry-led Corporate Governance Advisory Committee to promote good practices

FACILITATIVE FRAMEWORK
Aim: To support constructive and purposeful corporate governance practices
- Net reduction of 3 Principles and 31 Provisions
- More concise and less prescriptive, to encourage thoughtful application and move away from a box-ticking mindset
- Clarify expectations on compliance and acceptable variations from the Code

* To be shifted to the SGX Listing Rules
^ To be introduced in the Code of Corporate Governance for the first time

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Except for the rules on the 9-year cap on IDs and board composition of one-third IDs, the other changes will take effect for annual reports covering financial years starting January 1, 2019 onwards.

“The longer transition period accords companies sufficient time to ensure the composition of their boards is able to meet the requirements of the Listing Rules,” Singapore Exchange (SGX) explained.

On the new changes, Stefanie Yuen Thio, joint managing partner at TSMC Law Corporation, said: “The new CG Code focuses on what is important – the core principles of good governance – while streamlining and removing the plethora of rules which could encourage a ‘checklist mindset’ to governance.”

“For example, the requirements for a director to be considered ‘independent’ have been beefed up, because it is the role of independent directors to protect minority shareholders when their interests diverge from that of management or the majority shareholders,” Ms Thio said.

The fine tuned rules will help to ensure that directors do not have significant business or economic interests in the company, or entrenched boardroom friendships, that would compromise their objective decision-making, she added.

Ms Thio, who sits on the CG Council, believes the new Corporate Governance Advisory Committee will add clarity and flexibility for companies.

Corporate governance: More bouquets, but also more brickbats

SingTel tops SGTI ranking for fourth consecutive year with DBS Group a close second; CapitaLand, SGX in joint third

By Michelle Quah
michquah@sph.com.sg
@MichelleQuahBF

Singapore

AT first glance, this year’s Singapore Governance & Transparency Index (SGTI) points to a general improvement in corporate governance practices here.

But a closer examination of the scores reveals a telling rise in the amount of demerits handed out and, yet again, a yawning gap between the standards of top-ranked and bottom-ranked companies – all serving to remind investors to stay vigilant.

The SGTI, unveiled on Monday, is in its 10th year this year. It assesses listed entities on their corporate governance disclosures and practices, as well as the timeliness, accessibility and transparency of their financial results announcements.

A total of 589 Singapore-listed companies and 43 Reits and business trusts that released their annual reports by May 31 were ranked.

Listed companies were awarded a base score across five categories – board responsibilities, rights of shareholders, engagement of stakeholders, accountability and audit, and disclosure and transparency.

Bonus points are awarded for good practices, and penalty points docked for signs of poor corporate governance; each company had an overall score computed.

The average overall score for all listed companies has been on an uptrend since 2011, suggesting that corporate governance practices, when viewed across the entire market, have been improving.

This year, in particular, the score went up four points from last year, to 56.3.

Investors should, however, also look into the breakdown of this overall score, because it could alert them to specific instances or events that could dramatically change the ranking or scoring for companies, external circumstances or the environment in which a company operates can be as important as its internal practices and policies in deciding its performance.

For SGTI 2018, the average number of bonus points awarded to listed companies went up to 7.7 points, from 6.8 points last year.

However, the average number of penalty points awarded also rose.

The penalty scores went up to 10.2 this year, from an average of 9.0 last year.

The National University of Singapore Business School’s Centre for Governance, Institutions and Organisations (CGIO), which prepared the index, said penalty items are assigned on a company-specific basis and are usually event-triggered.

This is why companies in the embattled shipping industry, for example, and those hit with specific crises during the period, such as Keppel Corp, received more penalty points.

Real estate investment trusts (Reits) and business trusts were scored separately in the SGTI because of the unique nature of their operations. A decisive trend thus cannot yet be determined, given that these entities are being evaluated only for the second year in 2018.

Listed companies could stand to improve in certain specific areas. For a start, only a quarter (25.1 per cent) of them disclosed their CEO’s exact remuneration.

Under a 10th (9.7 per cent) engaged remuneration consultants to decide on directors’ remuneration this time around, down from 17.7 per cent in 2017.

CGIO said these ‘modest results’ suggest that companies need time to enforce the remuneration disclosures laid out in the new corporate governance standards.

It also found that companies could do better in the areas of director and board director training disclosures. Only 61.3 per cent of listed companies published their investor relations contact details on their website or in their annual report, which is 6.7 percentage points lower than the 68 per cent last year.

And, only 19.4 per cent of listed companies disclosed information on director training in 2018, down from 23.6 per cent in 2017.

Yeoh Oon Jin, Singapore divisional president in CFA Australia, which publishes the SGTI jointly with the CGIO and the Singapore Institute of Directors (SID), said: “Listed companies now operate in a disruptive and complex business environment and are increasingly under pressure to be more transparent and accountable to their stakeholders.

“Current corporate governance structures and processes need to evolve to remain relevant and effective in the future economy. With the SGTI, we hope that Singapore companies will continue their journey in strengthening governance locally, while aligning with global standards.”

There were many notable areas of improvement, however. The most laudable came from the top-ranked companies, as has been the case in previous years.

The SGTI found that the top 20 companies registered significant improvement in corporate governance, especially in stakeholder engagement, having better processes in board selection and standards of internal auditors.

SingTel topped the annual SGTI ranking in the general category for the fourth consecutive year. DBS Group was a close second, while CapitaLand and Singapore Exchange tied for third.

CGIO noted that United Overseas Bank made it into the top 10, in eighth place, for the first time, by showing strong improvements in the areas of board responsibility and disclosure and transparency. Singapore Press Holdings was ranked ninth after an eight year hiatus from the top 10.

CapitaLand Mall Trust led the Reit and business trust category for the second year. CapitaLand Commercial Trust took second spot, and Ascott Residence Trust, third.

Overall, stakeholder engagement scores and disclosures for code of conduct or ethics improved across the board.

SGTI also found improvements in board processes for director selection, appointments, training and re-election. For example, 64.5 per cent of companies disclosed their board diversity policy, compared to 33.7 per cent in 2017; 22.8 per cent had independent chairmanships, compared to 19.6 per cent in 2017.

The bulk (89.0 per cent) of listed companies revealed the provision of orientation programmes for new directors/commissioners, an improvement from 77.1 per cent in 2017.

CGIO said this is indicative of concerted efforts by companies to provide directors with a seamless transition into the roles and responsibilities of their assigned designation.

More companies have adopted the practice of re-electing directors every three years to allow shareholders to vote for director appointments regularly and to keep their board composition fresh.

They made up 84.4 per cent in 2018, from 78.5 per cent in 2017.

SID chairman Willie Cheng said: “It is heartening to note the steady, positive trajectory of corporate governance disclosures in Singapore, and the concerted effort by companies to improve on this front.

“With the latest changes to Listing Rules and Code of Corporate Governance, the bar is being raised, and we believe companies will embrace the tenets of good governance, including accountability, transparency and sustainability.”

“This includes establishing an appropriate culture, values and ethical standards of conduct at all levels of the company.”

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Progress in corporate governance, but challenges lie ahead

Addressing director tenure and board independence can also solve the problem of poor stakeholder engagement. BY LAWRENCE LOH

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S THE Singapore Governance and Transparency Index (SGTI) enters its fifth year of assessment, the remarkable progress made by companies over the years for this index, the average overall score for the general category of companies hits an all-time high of 56.3 from 33.9 in 2009. In the category of real estate investment trusts (REITs) and business trusts, there is a marked rise to 74.5 from 60.4 last year when this category was started.

The SGTI is based on a core assessment framework of five sections: (1) board responsibilities; (2) rights of shareholders; (3) engagement of stakeholders; (4) accountability and audit; and (5) disclosure and transparency. We examined the governance performance along these specific sections and found that companies generally performed well in the various sections, except the one on stakeholder engagement (see Figure 1). Notably, for companies in the general category, this section scored only 38 per cent even if it improved from 30 per cent last year.

Within the stakeholder engagement section, there were three more glaring omissions. These were: (1) disclosing policies and activities relating to customer health and safety; (2) publishing data on employee training and development; and (3) describing the company’s anti-corruption programs and procedures. In each of these separate aspects, only one-fifth of all companies in the general category fulfilled the assessment criteria. Beyond good overall progress of companies and the specific need for improvement in stakeholder engagement, let us look ahead at the critical concerns in the new corporate governance landscape when the Code of Corporate Governance and Singapore Exchange Listing Rules are revised. A most fundamental aspect that receives much attention is director tenure and board independence. For this year’s SGTI, we have an interesting range from new directors who just joined to the very seasoned directors who served more than 50 years (the director with the longest tenure is now on the board for some 55 years). Figure 2 shows the distribution of director tenure.

We made a fascinating observation that director tenure seems to have an impact on independent directors as shown in Figure 3. When director tenure increases, it seems that the proportion of independent directors decreases. We further examined whether companies making comprehensive assessment of the definition of director independence has any impact on director tenure. In a very revealing way, if companies do not make such independent definitions, directors tend to stay longer. On average, when independence definition is made, director tenure is 7.7 years compared to an increased 8.8 years when no such definition is made.

In fact, whether the chairman is independent or non-independent also affects the proportion of independent directors. Companies with independent chairmen have, on average, 54.6 per cent independent directors on the board whereas those with non-independent chairmen have 51.5 per cent.

The observations are very pertinent to gauge our companies’ readiness for a scenario when independent directors should form at least one-third of the board as well as the majority of the board if the chair is not independent. From the current proportion of independent directors in various situations, it appears that the companies are quite ready for the upcoming regulatory requirement. Nevertheless, it is critical to monitor director tenure and chairman independence on a continual basis so as to uphold the independence of boards.

Board independence has merits that are immense and multi-faceted. It is the highest assurance a company can be well-managed.

How scoring for the Index is done

THE Singapore Governance and Transparency Index (SGTI) is a joint initiative of CPA Australia, NUS Business School’s Centre for Governance, Institutions and Organisations (CGIO), and Singapore Institute of Directors. The strategic media partner is The Business Times.

Starting from 2017, the SGTI is a unified framework comprising two separate categories, namely the General Category and the REIT and Business Trust Category. These categories are distinct and are not to be compared directly with each other.

The objective of the SGTI is to evaluate listed companies, including REITs and Business Trusts, on their corporate governance practices and disclosures, as well as the timeliness, accessibility and transparency of their financial results. For the General Category, the SGTI score has two components: the base score, and the adjustment for bonuses and penalties. The base score for companies contains five sections: board responsibilities (35 points), rights of shareholders (30 points), engagement of stakeholders (10 points), accountability and audit (10 points), and disclosure and transparency (25 points). The aggregate of bonuses and penalties is incorporated in the base score to arrive at the company’s SGTI total score. For the REIT and Business Trust Category, the companies are evaluated on a similar set of criteria, but with added coverage on the unique nature of their operations.

The base score for REITs and Business Trusts includes items in the base score for the SGTI’s 65 points and trust-specific items in the base score for the SGTI for REITs and Business Trusts’ 65 points that focus on attractability, leverage, interested person transactions, competency of REIT manager/trustee manager, and compliance.

SGTI2018 covers 589 Singapore-listed companies in the General Category as well as 43 REITs and Business Trusts which released their annual reports by May 11, 2018.

The sources of information for SGTI2018 include annual reports, websites, announcements on SGXNet, and investor relations’ e-mail responsiveness. Assessments made on SGXNet as well as in media coverage, which occurred between Jan 1, 2016 and May 31, 2018, have been used to update the scores.

Further information on the scoring methodology, including the full instrument, and past results may be obtained from CGIO’s website at http://tech. nus.edu.sg/CGIO. Quotes about the SGTI may be sent to cjchua@nus.edu.sg. In order to maintain independence and fairness of the SGTI, reports or advice cannot be provided to individual companies.