



# The Singapore Directors' Toolkit

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## ► Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

# Foreword

Our business environment presents an ever-changing spectrum of risks and opportunities. The role of the director continues to be shaped by a multitude of forces including economic uncertainty, larger and more complex organisations, the increasing pace of technological innovation and digitisation, and a more rigorous regulatory environment. At the same time there is more onus on directors to operate transparently and be more accountable for their actions and decisions.

In Singaporean law, the board of directors is held to be ultimately responsible for virtually every aspect of the company's activities. However, it is impractical and undesirable for a board to attempt to supervise minutia associated with the company's operations.

Thus boards need to think carefully about their roles and functions and not meekly accept management agendas.

By understanding the environment and pressures the organisation and its management face, the board and audit committee (or equivalent) can assure itself that the material risks are being identified and most importantly, being managed. Such an approach enables the board and the audit committee to exercise its responsibilities in an active rather than a reactive manner and minimises 'surprises'. The board should be alert to the red flags or risk indicators that may impact the organisation's performance.

The Singapore Directors' Toolkit has been developed to support Directors in this challenging role. The Toolkit, in a user-friendly electronic format, cuts through the complexity of the regulatory environment whose

rules are captured in various key instruments such as The Singapore Companies Act, SGX Listing Rules and Singapore Code of Corporate Governance. The Toolkit pulls together all these requirements and is the only 'one-stop' electronic tool for Singapore directors to better understand their scope of work, roles and responsibilities and hence improve board performance and decision making.

This version of the Toolkit contains additional chapters to reflect issues which have risen in importance since the last edition in 2014. These include Social Media, Cyber Security, Sustainability and Workplace Health and Safety. It provides useful case studies of real-life examples on how to deal with complex and challenging issues.

We hope that you find this practical guide helpful to improve board performance and look forward to hearing your feedback.

**Irving Low**  
Head of Risk Consulting

## Foreword

- 01. Directors' Legal Duties
- 02. Structuring an Effective Board
- 03. Company Leadership
- 04. Productive Meetings
- 05. Ethical Culture
- 06. Board's Governance Roles and Conduct of Affairs
- 07. Insightful Strategy
- 08. Risk Management and Internal Controls
- 09. Board Committees
- 10. Receiving Assurance
- 11. Integrated Governance
- 12. Accountability to Shareholders
- 13. Stakeholder Engagement
- 14. Private Equity
- 15. Establishing a New Board
- 16. Managing Cybersecurity Risks
- 17. Corporate sustainability
- 18. Social media
- 19. Investment committees
- 20. Workplace safety & health
- 21. Appendices

# 1. Directors' Legal Duties

Company directors have significant legal responsibilities. It is critical to understand these duties, maintain compliance and continuously keep abreast of any relevant changes to regulations and guidance.

## Questions that company Directors should ask

- |   |  |
|---|--|
| 1. Do I have adequate working knowledge of the laws and regulations relevant to the company and the consequences of breaching them – including the Singapore Exchange (SGX) Listing Manual and Singapore Code of Corporate Governance 2012 (CG Code)? | 5. Is the Board immediately advised of queries received from the SGX or other regulators?                |
| 2. Does the Board receive reports from management about material changes to laws, regulations, Listing Manual and CG Code?  | 6. Are directors' interests properly disclosed?  |
| 3. Am I fully aware of my duties and responsibilities regarding conflicts of interest?  | 7. Do I understand the scope and limitations of the directors' and officers' liability insurance policy? |
| 4. Is there an effective procedure for identifying and disclosing related party transactions and interested party transactions?   | 8. Do I understand my responsibilities relating to company insolvency?                                   |
|   | 9. Am I confident that there are mechanisms in place to detect insider trading?                          |
|   | 10. Does the Company Secretary monitor compliance with the company Constitution?                         |

## Red flags

- |   |  |
|---|--|
| ► The company's Constitution is never, or rarely, referred to in Board discussions or documentation   | ► Insider trading by an employee is discovered, but no action is taken   |
| ► Certain directors are perceived to have conflicts of interest   | ► Concerns about certain directors or officers trading in company securities immediately before public announcements   |
| ► Concern that a family member of a director is a senior executive of a major supplier or customer  | ► The Board ignores a solvency problem and allows the business to continue trading or fails to seek further information in relation to the accounts when a reasonable director would do so |
| ► The directors fail to act in the best interests of the company as a whole (e.g. by having undue regard to the interests of a special interest group or major shareholder) | ► Insufficient time is paid to major decisions/ proposals or the annual financial statements   |
| ► A director lets price sensitive information slip  |  |



## Foreword

- **01. Directors' Legal Duties**
- 02. Structuring an Effective Board**
- 03. Company Leadership**
- 04. Productive Meetings**
- 05. Ethical Culture**
- 06. Board's Governance Roles and Conduct of Affairs**
- 07. Insightful Strategy**
- 08. Risk Management and Internal Controls**
- 09. Board Committees**
- 10. Receiving Assurance**
- 11. Integrated Governance**
- 12. Accountability to Shareholders**
- 13. Stakeholder Engagement**
- 14. Private Equity**
- 15. Establishing a New Board**
- 16. Managing Cybersecurity Risks**
- 17. Corporate sustainability**
- 18. Social media**
- 19. Investment committees**
- 20. Workplace safety & health**
- 21. Appendices**

Directors' responsibilities are regulated and guided by the following:

- Companies Act (Chapter 50) [CA]
- SGX Listing Rules [SGX LR]
- Individual company's Constitution
- Singapore Code of Corporate Governance 2012 [CG Code].

Additionally, there is a range of other legislative and regulatory regimes.

This includes the Banking Act, Securities and Futures Act (SFA), Income Tax Act, Workplace Safety and Health Act and Environmental Protection and Management Act. Company directors should be well-versed with the laws, regulations and rules applicable to the entities that they oversee.

This chapter provides an overview of some of the key duties; however, it is not intended as a comprehensive summation of all company officer and director duties. Directors should always seek legal advice if they are unsure about their legal position because circumstances can arise where they are held responsible for breaching certain laws, even when they did not specifically commit or authorise such a breach.

### Constitution

The power to control the affairs of the company is typically vested in the directors by the company's Constitution. The provisions of the Constitution are a key component of a company's governance framework. Directors should be familiar with the Constitution and take the necessary steps to ensure that it is understood, complied with and provides the appropriate framework for the operation of the company.

### SGX listing requirements

Companies and directors of companies listed on the SGX must comply with the listing rules<sup>1</sup>.

The listing rules are additional obligations imposed on listed companies, and govern the admission of entities to the SGX Mainboard and Catalist Board, the quotation of entities' securities, continuous disclosure obligations, directors' disclosures, suspension of securities from quotation and the removal of entities from the official list. The listing rules are enforceable against listed entities.

### Key duties and responsibilities

A "director" is defined to include any person occupying the position of director of a corporation and includes a person in accordance with whose directions or instructions the directors of a corporation are accustomed to act. This would include de facto, shadow, alternate, independent, nominee, executive and non-executive directors<sup>2</sup>.

A director is responsible for providing the direction for the company. Directors must act in good faith and objectively make decisions in the best interests of the company.

<sup>3</sup> They must also exercise diligence in carrying out their duties and should avoid conflicts of interest<sup>4</sup>. In addition, Directors must only exercise their powers for proper purposes and should not use their position or information acquired by virtue of their position to gain an advantage for themselves or others, or cause detriment to the company.<sup>5</sup>

Director's duties are primarily contained within common law and statutory obligations (within the Companies Act).

<sup>1</sup> SGX LR 101, 102 & 209

<sup>2</sup> CA Section 4(1)

<sup>3</sup> CG Code Principle 1.2

<sup>4</sup> CA Section 157 & Section 156

<sup>5</sup> CA Section 157



## Foreword

### ► 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

Whilst the law provides that a director's duty is owed to 'the company', the courts have typically characterised the company as being the sum of the shareholders.

Though directors' legal duties are narrowly defined in this sense, there is a growing public expectation that directors will take account of community interests and accede to the notion of 'corporate social responsibility'.

A director owes his duties to the

- Company - duties are owed to the company and not to members of the company individually. Only the company may commence legal proceedings against a director for any breaches of duties
- Shareholders - duties owed to shareholders to act in their best interests
- Creditors - a director must also take into consideration the interests of the creditors to ensure that the assets of the company are not improperly dissolved or its affairs improperly managed, especially in the case of insolvency, or the threat of insolvency<sup>6</sup>
- Employees - directors must consider the interests of the employees when exercising their powers<sup>7</sup>

Directors play imperative roles in steering and controlling the company and hence are subjected to roles and responsibilities, as detailed below:

*Fiduciary duties: to act in good faith and in the best interests of the company*

Directors and officers of a company are under a statutory and common law duty to act in good faith and in the best interests of the company, and for a proper purpose. This

duty recognises that a director's primary responsibility is to the company and that this responsibility must ordinarily take precedence over the personal interests of the director and that of third parties. The duty to act in good faith is a broad duty that requires directors to:

- exercise their powers only for proper corporate purposes
- avoid actual, potential and perceived conflicts of interest
- objectively make decisions in the interest of the company
- account to the company for business opportunities that arise.

Directors must also not act beyond powers given in the Constitution, illegally or contrary to public policy.

In addition, an offence is committed under both statute and common law if it can be shown that any conduct was undertaken without good faith. It is not necessary to establish that the advantage was actually obtained.

*Duty to exercise care and diligence reasonably expected of them*

Directors must exercise their duties with the degree of care and diligence that a reasonable person would exercise if they were a director of the company and occupied the same responsibilities within the company as the director.

The courts, in determining a director's duty of care and skill, have employed the use of an objective and subjective test.

<sup>6</sup> CA Section 159

<sup>7</sup> CA Section 159

## Foreword

### ► 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

While the objective test would take into account the general knowledge, skill and experience which may be reasonably expected of a person carrying out the same functions as the director, the subjective test would hold the director to higher standards by examining factors specific to the director, such as his experience and expertise.

Furthermore, a diligent director would be expected to seek the advice of other fellow directors or a professional advisor on matters that he is not familiar with and make proper enquiries about the company's business where needed<sup>8</sup>.

Some of the examples where the duty of care and skill may not be satisfied:

- Signing circulating resolutions because others have signed it
- Attending Board meetings without reading papers
- Failing to make further enquiries/seek more information when in doubt about certain matters, such as:
  - Company is venturing into new business sector and only cursory information about the new business is provided
  - Knowing that some directors and senior officers have excessive entertainment expenses
  - New laws are being introduced and not checking to see how they could impact the company.

### *Business judgement rule*

There is no formal 'business judgement rule' contained within the Companies Act. However, as established through case law:

"The courts should be slow to interfere with commercial decisions taken by directors. It should not, with the advantage of hindsight, substitute its own decisions in place of those made by directors in the honest and reasonable belief that they were for the best interests of the company, even if those decisions turned out subsequently to be money-losing ones..."<sup>9</sup>

The 'business judgement rule' provides a measure of protection for directors, who may otherwise be in breach of the duty of care and diligence for poor business decisions.

Incompetence is not considered a breach of fiduciary duty even though it may attract other types of liability. Without evidence of a lack of acting in good faith, it cannot be contended that directors are invariably liable by their failure in business judgment for all losses sustained by a company.<sup>10</sup>

However, the business judgement rule does not protect a cavalier attitude to business risk. Directors are expected to make informed business judgements and they must have a rational belief that their decisions are in the best interests of the company. The director's belief that the judgement is in the best interests of the company is a rational one, unless the belief is one that no reasonable person in their position would hold. This means that directors should exercise their powers and discharge their duties with the degree of care and diligence expected of any reasonable person in their position.

<sup>8</sup> Jurong Readymix Concrete Pte Ltd v Kaki Bukit Industrial Park Pte Ltd [2000] 4 SLR 723

<sup>9</sup> ECRC Land Pte Ltd v Ho Wing On Christopher and Others  
<sup>10</sup> Vita Health Laboratories Pte Ltd & Ors v Pang Seng Meng [2004] 4 SLR(R) 162

## Foreword

- ▶ **01. Directors' Legal Duties**
- 02. Structuring an Effective Board**
- 03. Company Leadership**
- 04. Productive Meetings**
- 05. Ethical Culture**
- 06. Board's Governance Roles and Conduct of Affairs**
- 07. Insightful Strategy**
- 08. Risk Management and Internal Controls**
- 09. Board Committees**
- 10. Receiving Assurance**
- 11. Integrated Governance**
- 12. Accountability to Shareholders**
- 13. Stakeholder Engagement**
- 14. Private Equity**
- 15. Establishing a New Board**
- 16. Managing Cybersecurity Risks**
- 17. Corporate sustainability**
- 18. Social media**
- 19. Investment committees**
- 20. Workplace safety & health**
- 21. Appendices**



## Case Study

Mr. Ngu Tieng Ung and Mr. Tang Kok Heng were directors of Firstlink Energy Pte Ltd ("Firstlink"), while Mr. Tang was also the majority and controlling shareholder of Creanovate Pte Ltd ("Creanavote"). Mr. Tang had written to Firstlink Energy to propose a Joint Venture Agreement (JVA) in a coal-mining venture. \$4.26 million was advanced by Firstlink Energy to Creanovate under a subscription agreement, but the conditions precedent under that agreement were not fulfilled in time.



Firstlink then sued Creanovate for the return of the monies. In addition, Mr. Ngu and Mr. Tang were also sued for breaching their fiduciary duties by allowing the advancement of the monies. In fact, there was evidence of the duo using the \$4.26 million for their own benefit. The monies were first banked in, and then diverted to Mr. Ngu and Mr. Tang's accounts,

and in several occasions, for payment to Mr. Ngu's stockbrokers.

The Court determined there were clear breaches of fiduciary duties made by Mr. Ngu and Mr. Tang as directors of Firstlink Energy, and found the directors had misappropriated company funds for their own use. Both Mr. Ngu and Mr. Tang were liable for the sum.

However, when a Board of Directors have made an honest decision that did not prove to be a good one, they cannot be accused of having breached their fiduciary duties, as in the case of *Intraco Ltd v Multi-Pak Singapore Pte Ltd* [1995] 1 SLR 313. Multi-Pak issued shares to Intraco in return for a debt owed to Intraco by City Carton, a company related to Multi-Pak. City Carton was not likely to repay the debt and hence, the transaction did not appear to be beneficial to Multi-Pak. When the case was challenged, the court recognised that there was a benefit to Multi-Pak in forming a strategic business alliance with Intraco and therefore held that there was no breach of directors' duties involved.

The two cases highlight the difference between acting without good faith and not in the best interests of the company, and an honest but poorly made decision that was acted out in good faith by directors. While directors are liable for breaches of trust and failure to act honestly and with reasonable diligence, the Court recognises that circumstantial changes may render a decision made in the best interests of the company to have the opposite effect.



## Foreword

### ► 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

### *Statutory duties*

Aside from acting honestly and diligently in the discharge of duties, Directors have to comply with disclosure and other requirements. Duties for disclosure and other requirements stated in the Companies Act include:

- S165 General duty to make disclosure. A listed company has a duty under the SGX LR to immediately announce, upon receipt of notifications from its directors, their disclosable interests and changes thereof
- S156 Duty to disclose interests in transactions (examples include interests in property or offices which may create conflicts of interest)
- S164 Duty to disclose director's shareholdings (examples include shares, rights or options, debentures and contracts in the company or a related corporation)
- S160 Duty to seek approval – disposal of undertaking or property
- S171 Duty to appoint secretaries and auditors
- S175 Duty to hold Annual General Meetings (AGM)
- S197 Duty to file annual returns
- S199 Duty to maintain proper accounting records
- S201 Duty to present audited accounts at AGM. Accounting records must comply with Accounting Standards.

Common defaults of statutory duties include failure to hold an AGM<sup>11</sup>, failure to file annual returns<sup>12</sup>, failure to file changes in particulars, especially resignation of directors<sup>13</sup> and change in company's registered office address<sup>14</sup>.

The SGX LR Chapter 7 sets out the continuing disclosure requirements with which a listed company has to comply.

Reference should also be made to SGX's Corporate Disclosure Policy in Appendix 7.1.

### *Conflict of interests and disclosure*

Conflict of interest situations and disclosure requirements are governed by both common law and statutory law. One fundamental difference between the two is the disclosure requirements when handling such matters. While common law requires disclosure to and approval from a general meeting, statutory disclosure requirements only require appropriate disclosure to the Board. In addition, because of the practical obstacles to the common law disclosure rule, the company's Constitution may modify the rule by including regulations stating that compliance with statutory disclosure requirements are sufficient. Therefore, directors should pay special attention to the company's Constitution, as well as:

- Provisions of the CA, and in particular, whether the situation falls within any specific provision of the Act prohibiting or prescribing procedures in relation to the relevant situation of conflict, for example restrictions are placed on a company granting loans to directors<sup>15</sup>
- SGX LR Chapter 9 Interested Person Transactions

11 CA Section 175

12 CA Section 197

13 CA Section 173

14 CA Section 143

15 CA Section 163

## Foreword

- 01. Directors' Legal Duties
- 02. Structuring an Effective Board
- 03. Company Leadership
- 04. Productive Meetings
- 05. Ethical Culture
- 06. Board's Governance Roles and Conduct of Affairs
- 07. Insightful Strategy
- 08. Risk Management and Internal Controls
- 09. Board Committees
- 10. Receiving Assurance
- 11. Integrated Governance
- 12. Accountability to Shareholders
- 13. Stakeholder Engagement
- 14. Private Equity
- 15. Establishing a New Board
- 16. Managing Cybersecurity Risks
- 17. Corporate sustainability
- 18. Social media
- 19. Investment committees
- 20. Workplace safety & health
- 21. Appendices

### *Conflict Rule and Personal Interest Conflict*

The general law conflict rule states that directors must not place themselves in a position where there is an actual or substantial possibility of conflict between personal interest and their duty to act in the interests of the company. A common scenario of such conflict is where directors have a direct or indirect material interest in transactions that the company is undertaking or considering.

In such cases, it is important to note that the interests of the director's family are treated as director's interest, and it is required of directors to disclose the conflict and seek approval in accordance to the common law disclosure rule, as well as statutory disclosure requirements, regardless of whether the director profits or the company suffers a loss.<sup>16</sup>

### *Duty-duty Conflict*

Under common law, a director's duty not to place himself in a position where the director's duty to the company may possibly conflict with his duty to someone else. The following are common scenarios:

- *Directors holding directorship in two companies.*  
While there is no legal rule prohibiting directors from taking up multiple directorships, under common law, where there is an actual or substantial possibility of conflict between two duties, directors must disclose the potential conflict and not engage in any action or decision for either company in relation to the matters – adopting a "remain above the fray" stance.

Statutorily, a director is required to make disclosure if he holds any office or property where his duty or interests are in conflict with his duties as a director in the company.

- *Nominee directors*

Nominee directors may be in breach of their duty to act in the best interests of the company or, their duty not to make improper use of information, when they inform their appointers of confidential matters that might impact the interest of their appointers.

To assist nominee directors in their appointments, under Section 158 of the CA, they are allowed to disclose information they possess by virtue of their position as directors or employees to:

- A person whose interest the director represents; or
- A person in accordance with whose instructions the director may be required to act;

if such disclosure is not likely to prejudice the company and is made with the authorisation of the Board.

### *Profit Rule*

Similar to the general law conflict rule is the profit rule, where a person in a fiduciary position is not entitled to profit by reason of and in the course of his fiduciary position without adequate disclosure to and approval from a general meeting. It should be noted that the profit rule is not to be construed as a subset of the conflict rule, and a director can be pursued under the profit rule even when he may not have been in breach of the conflict rule.

16 CA Section 156(1)

## Foreword

- **01. Directors' Legal Duties**
- 02. Structuring an Effective Board**
- 03. Company Leadership**
- 04. Productive Meetings**
- 05. Ethical Culture**
- 06. Board's Governance Roles and Conduct of Affairs**
- 07. Insightful Strategy**
- 08. Risk Management and Internal Controls**
- 09. Board Committees**
- 10. Receiving Assurance**
- 11. Integrated Governance**
- 12. Accountability to Shareholders**
- 13. Stakeholder Engagement**
- 14. Private Equity**
- 15. Establishing a New Board**
- 16. Managing Cybersecurity Risks**
- 17. Corporate sustainability**
- 18. Social media**
- 19. Investment committees**
- 20. Workplace safety & health**
- 21. Appendices**

### *Taking of corporate information and opportunity*

Directors cannot take property, information or opportunity belonging to the company, without the permission of the company. This duty would, for example, prohibit a director from obtaining a personal benefit through the misuse of the company's client or supplier list.

More specifically, in the case of taking of corporate opportunity, the following should be used:

- No-conflict analysis: A director should not take a business opportunity that the company is itself considering, or opportunities that the company is reasonably expected to be interested in, given its current line of business
- No-profit analysis: An officer shall be accountable for profit arising by reason of and in the course of his fiduciary office

The dual-pronged analysis allows for directors to fully comprehend and examine their responsibilities in scenarios that may constitute taking of corporate opportunity:

|  | No-conflict analysis   | No-profit analysis  |
|--|--|---|
| What if the company is not in a position to take up the opportunity? | Nonetheless, if the company is reasonably expected to be interested in the opportunity, directors still cannot take up the opportunity without the necessary disclosure and approval | If the opportunity arose by virtue of the director's position, he is not entitled to profit from it without adequate disclosure and approval          |
| What if the director resigns to take up the opportunity?             | There is still a breach of the conflict rule, if the resignation was prompted or influenced by a desire to acquire the opportunity sought by the company                             | If the opportunity arose by virtue of the director's position, he is not entitled to profit from it without adequate disclosure and approval          |
| What if the company has, in good faith, rejected the opportunity?    | In the case of good faith rejection, the company is no longer interested in the opportunity, and the director may take it up without breaching the conflict rule                     | However, if the opportunity arose by virtue of the director's position, he is not entitled to profit from it without adequate disclosure and approval |



## Foreword

- **01. Directors' Legal Duties**
- 02. Structuring an Effective Board**
- 03. Company Leadership**
- 04. Productive Meetings**
- 05. Ethical Culture**
- 06. Board's Governance Roles and Conduct of Affairs**
- 07. Insightful Strategy**
- 08. Risk Management and Internal Controls**
- 09. Board Committees**
- 10. Receiving Assurance**
- 11. Integrated Governance**
- 12. Accountability to Shareholders**
- 13. Stakeholder Engagement**
- 14. Private Equity**
- 15. Establishing a New Board**
- 16. Managing Cybersecurity Risks**
- 17. Corporate sustainability**
- 18. Social media**
- 19. Investment committees**
- 20. Workplace safety & health**
- 21. Appendices**

Directors should exercise caution when considering fellow directors' actual, potential or perceived conflicts of interest. Conflicts of interest may not be avoidable at times given the more complex business environment in which companies now operate. An actual or potential conflict does not necessarily disqualify a person from serving on a company's Board, but full disclosure should be made and where required by law, shareholders' approval should be obtained to guard the best interests of the company and its shareholders.

Where such a situation is unavoidable, and creates a conflict with the director's fiduciary duties to the company, approval should be obtained from which the shareholders or immediate announcement made in circumstances specified by Chapter 9 of the SGX LR.

Related party transactions should be disclosed in the annual report in accordance with Financial Reporting Standard 24. Measures need to be taken to avert any adverse consequences to the company. An offence is committed under statute and SGX LR if it can be established that the conduct was undertaken with the intention of gaining personal advantage; it is not necessary to determine that an actual gain was obtained.

Statement of Good Practice (SGP) No. 5/2006 provides further guidance. Where there are uncertainties as to whether or not the directors are in a position of conflict, the matter should be deliberated with the Chairman of the Board or the Nominating Committee (NC). If necessary, professional advice should be sought and where there is still reasonable doubt after such consultation, the issue should be treated as a conflict situation.

The Company Secretary, upon notification by the directors should inform the Board of the conflict by circular as soon as is practicable. Formal disclosure of the conflict should then be made and minuted at the next Board meeting. Listed companies are to disclose in their annual reports particulars of material transactions between their CEOs, directors and controlling shareholders with the companies or their subsidiaries.

In determining whether or not a particular transaction is material, directors should take into account the value and nature of the transaction and the impact that the transaction may have on the company. Where there is no such transaction, a negative statement to that effect must be disclosed in the annual report.

Whether or not a director is permitted to be present at a meeting when discussing matters, in which he has a conflict of interest, depends on the company's Constitution.

However, in the absence of any prohibition in the Constitution, directors are allowed to be present at the meeting when the subject matter to which the conflict relates is discussed, although conflicted directors are encouraged to excuse themselves when the conflicted-related matter is reviewed for impartiality unless the Board views that his presence and participation is necessary to enhance the effectiveness of such discussion. When it comes to voting, the SGX LR prohibits directors from voting where the contract or proposed contracts in which the directors have, directly or indirectly, a personal material interest<sup>17</sup>.

17 SGX LR 409, Appendix 2.2 (9)(e)

## Foreword

- **01. Directors' Legal Duties**
- 02. Structuring an Effective Board**
- 03. Company Leadership**
- 04. Productive Meetings**
- 05. Ethical Culture**
- 06. Board's Governance Roles and Conduct of Affairs**
- 07. Insightful Strategy**
- 08. Risk Management and Internal Controls**
- 09. Board Committees**
- 10. Receiving Assurance**
- 11. Integrated Governance**
- 12. Accountability to Shareholders**
- 13. Stakeholder Engagement**
- 14. Private Equity**
- 15. Establishing a New Board**
- 16. Managing Cybersecurity Risks**
- 17. Corporate sustainability**
- 18. Social media**
- 19. Investment committees**
- 20. Workplace safety & health**
- 21. Appendices**

## DIRECTORS' LEGAL DUTIES

A director's independence needs to be carefully considered during re-appointment, with regard to the conflict of interest situations. Voluntary resignation is also an option where a continuing material conflict of interest may possibly affect the director's duty to the company. It is, however, encouraged that the directors try to resolve the matter.

An important point to note in this area is that the stakeholders and the media can be highly critical of director conduct that can be perceived as self-serving – the securities markets can jump to hasty conclusions when public opinion starts demanding resignations. The reputations of both individual directors and their companies can suffer dramatically.

Some instances in which there are perceptions that directors and managers have been too closely involved in private equity bids for their companies have attracted criticism. Directors need to exercise caution where the potential for personal gain is, or could be seen to be, in conflict with the best interests of the company and its shareholders.



## Case Study

In the 2000 case of *Public Prosecutor v Yeo Geok Seng*, the Honourable Chief Justice Yong Pung How upheld the conviction of Mr. Yeo as a director, under Sections 156(5) and 156(1) of the Singapore Companies Act (Cap 50), for his failure to make disclosures required under section 156, when the company transacted with other companies in which he had an interest as director or shareholder.



## Foreword

- **01. Directors' Legal Duties**
- 02. Structuring an Effective Board**
- 03. Company Leadership**
- 04. Productive Meetings**
- 05. Ethical Culture**
- 06. Board's Governance Roles and Conduct of Affairs**
- 07. Insightful Strategy**
- 08. Risk Management and Internal Controls**
- 09. Board Committees**
- 10. Receiving Assurance**
- 11. Integrated Governance**
- 12. Accountability to Shareholders**
- 13. Stakeholder Engagement**
- 14. Private Equity**
- 15. Establishing a New Board**
- 16. Managing Cybersecurity Risks**
- 17. Corporate sustainability**
- 18. Social media**
- 19. Investment committees**
- 20. Workplace safety & health**
- 21. Appendices**

### Related Party Transactions (RPT) and Interested Person Transactions (IPT)

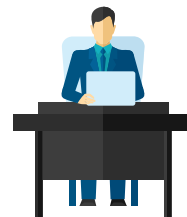
In Singapore, Interested Person Transactions (IPTs) and Related Party Transactions (RPTs) are governed by Chapter 9 of the SGX LR and FRS 24 Related Party Disclosures respectively.

While both types of transactions may adversely affect the interests of shareholders, they should not be termed interchangeably as their definitions differ and they attract dissimilar disclosure requirements.

In the case of IPTs, Chapter 9 of the SGX LR defines an interested person to be a director, chief executive officer, or controlling shareholder of the issuer; or an associate of any such director, chief executive officer, or controlling shareholder<sup>18</sup>.

The SGX LR outlines the procedure to announce any interested person transaction of a value equal to, or more than, 3% of the group's latest audited net tangible assets (NTA). Shareholders' approval needs to be sought when IPTs of a value equal to, or more than, 5% of the group's latest audited net tangible assets (NTA). The rule does not apply to any transaction below S\$100,000<sup>19</sup>.

A brief illustrative diagram of the common scenarios that constitute an IPT covered under Chapter 9 of the SGX LR is shown below:



#### Interested Person

- Director, CRO or controlling shareholder of the listed company
- Associate of director, CEO or controlling shareholder



#### Entity at Risk

#### Transaction

- Provision or receipt of financial assistance
- Acquisition, disposal or leasing of assets
- Provision or receipt of services
- Issuance or subscription of securities
- Granting or being granted options
- Establishment of joint ventures or joint investments

- Listed company
- Unlisted subsidiary
- Unlisted associated company, where the listed issuer together with interested person(s) control the associate company

<sup>18</sup> SGX LR 904

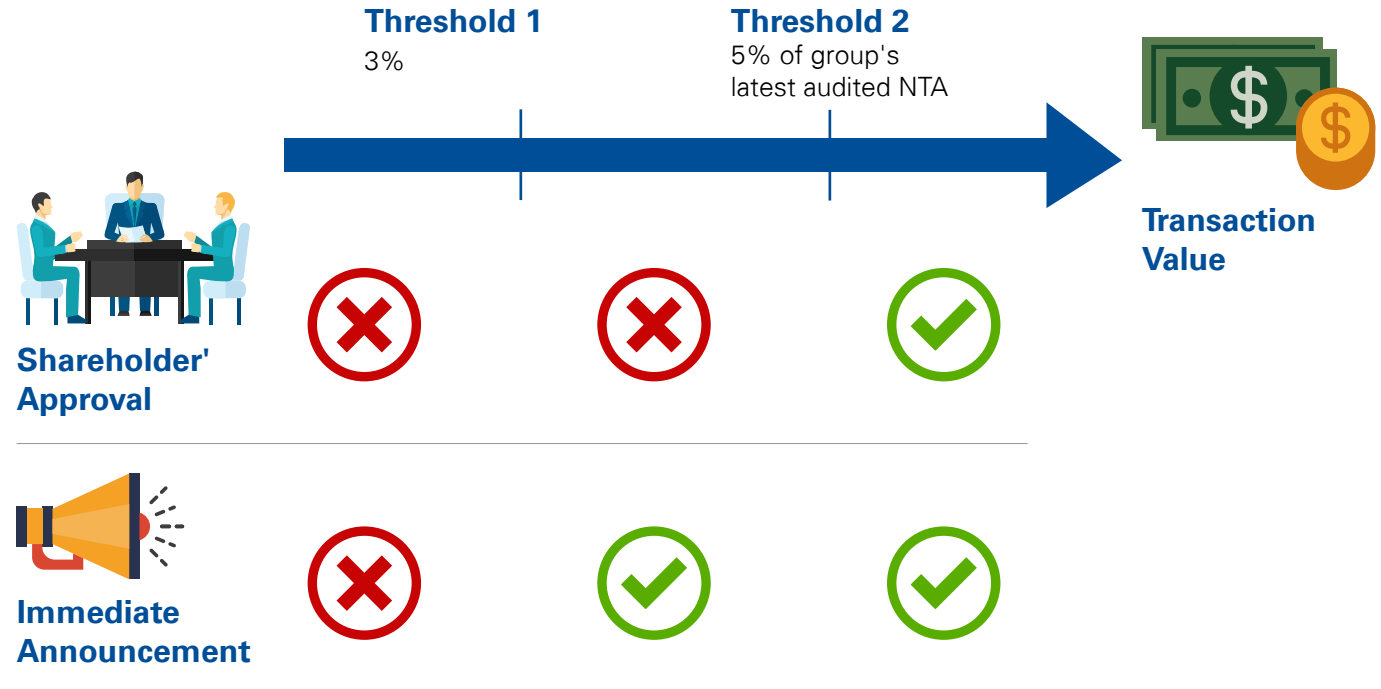
<sup>19</sup> SGX LR 905 & 906



## Foreword

- ▶ 01. Directors' Legal Duties
- 02. Structuring an Effective Board
- 03. Company Leadership
- 04. Productive Meetings
- 05. Ethical Culture
- 06. Board's Governance Roles and Conduct of Affairs
- 07. Insightful Strategy
- 08. Risk Management and Internal Controls
- 09. Board Committees
- 10. Receiving Assurance
- 11. Integrated Governance
- 12. Accountability to Shareholders
- 13. Stakeholder Engagement
- 14. Private Equity
- 15. Establishing a New Board
- 16. Managing Cybersecurity Risks
- 17. Corporate sustainability
- 18. Social media
- 19. Investment committees
- 20. Workplace safety & health
- 21. Appendices

A brief illustrative diagram of the required disclosure and approval for the common scenarios that constitute an IPT covered under Chapter 9 of the SGX LR is shown below:



A 2013 survey by KPMG and NUS<sup>20</sup>, found that the most common type of IPT relationship is that between a controlling shareholder and an associate. 23% of these transactions were between the entity at risk and an associate of a director. When compared to IPTs directly involving a director or a controlling shareholder, IPTs involving their associates may face a greater risk of not being properly identified and may result in potential unintentional omission of significant IPTs. It is therefore important for directors to ensure that the company has

robust internal processes in place to identify associates of the controlling shareholder, directors and the CEO.

An example of such a process would be establishing a register of directors' IP associates and then requiring them to update the register if and when there were any changes. Each director would then be required to sign an annual declaration that they have disclosed all their IP relationships and changes on a timely basis.

In the case of RPTs, FRS 24's definition of a "related party" is wider than that of an "interested person"

<sup>20</sup> The Ties That Bind: Interested Person Transactions: Rules and Practices, KPMG and NUS Publication, September 2013, page 22

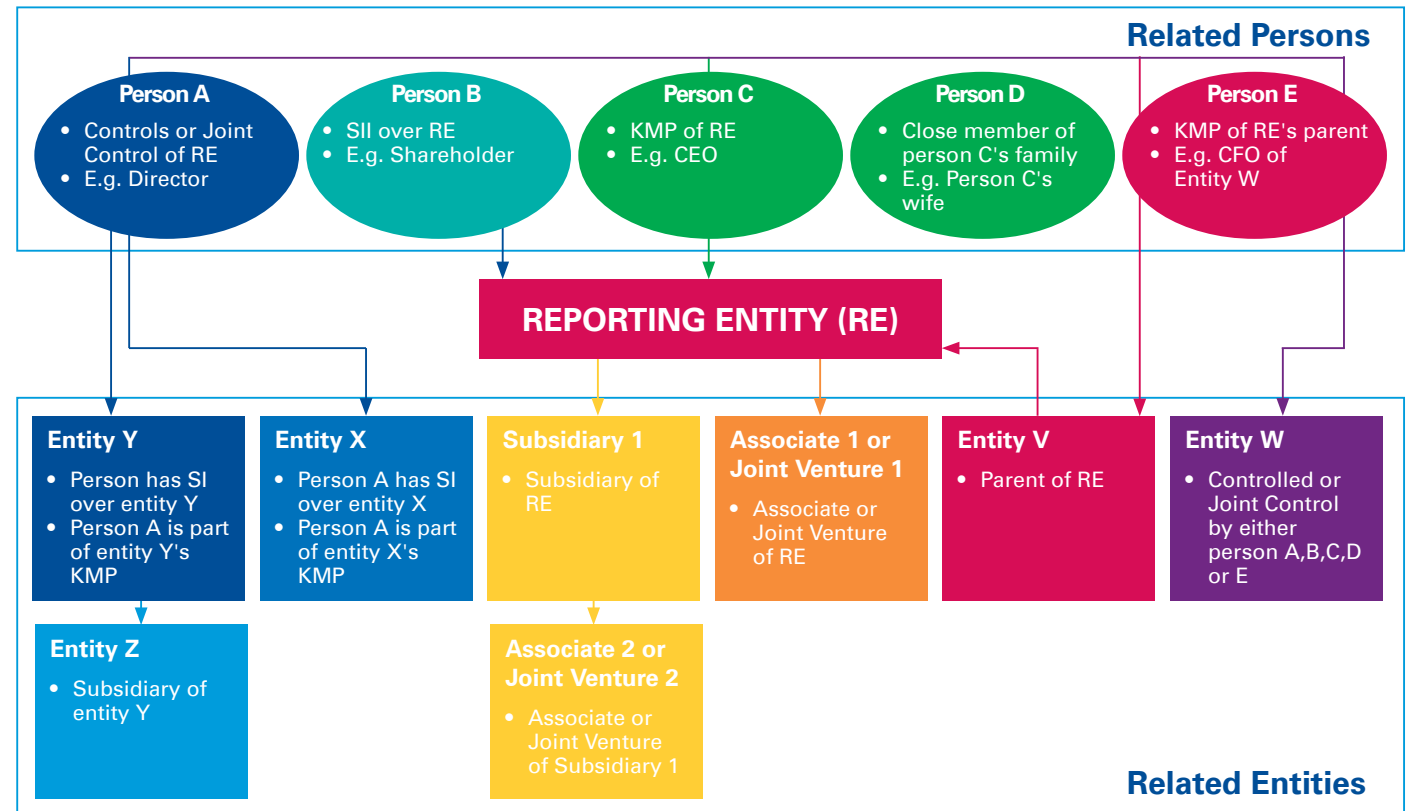
## Foreword

- 01. Directors' Legal Duties
- 02. Structuring an Effective Board
- 03. Company Leadership
- 04. Productive Meetings
- 05. Ethical Culture
- 06. Board's Governance Roles and Conduct of Affairs
- 07. Insightful Strategy
- 08. Risk Management and Internal Controls
- 09. Board Committees
- 10. Receiving Assurance
- 11. Integrated Governance
- 12. Accountability to Shareholders
- 13. Stakeholder Engagement
- 14. Private Equity
- 15. Establishing a New Board
- 16. Managing Cybersecurity Risks
- 17. Corporate sustainability
- 18. Social media
- 19. Investment committees
- 20. Workplace safety & health
- 21. Appendices

as it covers key management personnel, close family members, corporate entities with control, joint control, common control or significant influence ties and certain of their connected persons. Related party transaction disclosure requirements apply to public companies, or entities controlled by a public company, and there are

significant procedural steps involved in managing such transactions which are designed to protect shareholders' interest. A related party transaction is a transfer of resources, services or obligations between a reporting entity and a related party, regardless of whether a price is charged<sup>21</sup>.

A summary of entities or persons that constitute related parties under FRS 24 is illustrated below:



- KMP refers to Key Management Personnel
- SI refers to Significant Influence
- Ellipses are used to represent: 'Persons', while boxes represent entities

\*Person D may be also a close member of person A, B or E's family. In this illustration, the example of Person D being Person C's wife was used. It should be noted that close members of Person A, B or E's family will be deemed to be related to the RE as well. (E.g. Person A's child is considered related person to the Reporting Entity)

## Foreword

### ► 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

FRS 24 requires entities to disclose these transactions:<sup>22</sup>

(a) Key Management Personnel compensation includes:

- Short-term employee benefits - wages, salaries and social security contributions, paid annual leave and paid sick leave, profit-sharing and bonuses and non-monetary benefits for current employees
- Post-employment benefits - pensions, other retirement benefits, post-employment life insurance and post-employment medical care
- Other long-term benefits - long-service leave or sabbatical leave, jubilee or other long-service benefits, long-term disability benefits and, if they are not payable wholly within 12 months after the end of the period, profit sharing and deferred compensation:
  - Termination benefits
  - Share-based payments

(b) Other transactions

FRS 24 requires that if there have been transactions between related parties, an entity shall disclose the nature of the related party relationships as well as information about the transactions and outstanding balances, including commitments, necessary for an understanding of the potential effect of the relationship on the financial statements.

Importantly, because FRS 24 is used for financial reporting purposes, it stipulates that 'in considering each possible related party relationship, attention is directed to the substance of the relationship and not merely the legal form'.<sup>23</sup>

22 Guidebook for Audit Committees in Singapore (2<sup>nd</sup> Edition)

23 Guidebook for Audit Committees in Singapore (2<sup>nd</sup> Edition)



## Foreword

- **01. Directors' Legal Duties**
- 02. Structuring an Effective Board**
- 03. Company Leadership**
- 04. Productive Meetings**
- 05. Ethical Culture**
- 06. Board's Governance Roles and Conduct of Affairs**
- 07. Insightful Strategy**
- 08. Risk Management and Internal Controls**
- 09. Board Committees**
- 10. Receiving Assurance**
- 11. Integrated Governance**
- 12. Accountability to Shareholders**
- 13. Stakeholder Engagement**
- 14. Private Equity**
- 15. Establishing a New Board**
- 16. Managing Cybersecurity Risks**
- 17. Corporate sustainability**
- 18. Social media**
- 19. Investment committees**
- 20. Workplace safety & health**
- 21. Appendices**



## Case Study

SGX issued several queries to China Sky in 2010, including one on an accounting service provider, SK Lai & Co. which provided significant accounting-related services to the Company. SK Lai & Co. was founded by Mr. Lai Seng Kwoon, who was, at that time, an independent director and Chairman of the company's Audit Committee. The amount of fees involved suggests that the work of his firm was substantial, which raised an issue of the conflict between his role as the Audit Committee Chairman and his firm's role in providing accounting-related services.



In a 2010 corporate governance report, China Sky' had asserted Mr. Lai's independence and stated that the independent directors have confirmed they do not have any relationship that could interfere with their business judgment. While China Sky maintained that Interested Party Transactions were "conducted at arm's length", the SGX questioned why the services of SK Lai & Co. were engaged, when there were many other accounting firms that could have provided similar services.

Mr. Lai was arrested in 2012 by the Commercial Affairs Department and had his passport impounded. In 2013, Stone Forest, the auditors appointed to conduct a special audit confirmed that the relationship between Mr. Lai's accounting services firm and China Sky constituted an IPT.

## Foreword

- 01. Directors' Legal Duties
- 02. Structuring an Effective Board
- 03. Company Leadership
- 04. Productive Meetings
- 05. Ethical Culture
- 06. Board's Governance Roles and Conduct of Affairs
- 07. Insightful Strategy
- 08. Risk Management and Internal Controls
- 09. Board Committees
- 10. Receiving Assurance
- 11. Integrated Governance
- 12. Accountability to Shareholders
- 13. Stakeholder Engagement
- 14. Private Equity
- 15. Establishing a New Board
- 16. Managing Cybersecurity Risks
- 17. Corporate sustainability
- 18. Social media
- 19. Investment committees
- 20. Workplace safety & health
- 21. Appendices

### Insider trading

Insider trading involves the misuse of price or value sensitive company information that is not generally available to the public. By virtue of directors' roles, they will be privy to inside information and should take steps to ensure that prohibition against insider trading in the SFA is carefully observed.

Insider trading liability is based not on whether a person trading on price-sensitive information is connected with the relevant company but whether the person is in possession of price-sensitive information. If in possession of such information, the person is prohibited from trading<sup>24</sup>. The Act specifies that an officer of the company shall not make improper use of any information acquired by virtue of his position to gain, directly or indirectly, an advantage for himself or for any other person or to cause detriment to the company<sup>25</sup>.

The following situations represent a breach of insider trading requirements<sup>26</sup>:

- A director buying or selling securities of the company while in possession of any inside information concerning the company
- A director procuring another person to buy or sell securities of the company while in possession of inside information
- A director communicating the information, or causing the information to be communicated, to another person who is likely to trade in those financial products

Insider trading is a serious offence attracting substantial fines and potential imprisonment.

To prevent potential misuse of the director's powers, the Act now requires directors to obtain the approval of the company in a general meeting prior to exercising any power of the company to issue shares<sup>27</sup>.

<sup>24</sup> SFA Section 218

<sup>25</sup> CA Section 157(2)

<sup>26</sup> SFA Section 218

<sup>27</sup> CA Section 161



## Case Study

In 2011, the former Chief Operating Officer (COO) of Airocean, Johnson Chong, was found guilty on the charges of insider trading, with the ruling stating that evidence 'clearly showing that as a connected person, he was aware and knew or ought to have known that the 'relevant information' which was available to him was price-sensitive and not generally available'. The charge was in respect of the breach of Section 218(2)(a) of the SFA.



In finding Mr. Chong guilty on the charges of insider trading, the judge wrote, "When the trades were conducted, the public did not know the above information, Mr. Chong agreed that he had an informational advantage over other members of the public at the time when he sold the shares."

Mr. Chong was sentenced to four months' jail for insider trading and was disqualified from acting as a director for 5 years<sup>28</sup>.

<sup>28</sup> <http://www.mondaq.com/x/134508/Directors+Officers+Executives+Sha>

## Foreword

- 01. Directors' Legal Duties
- 02. Structuring an Effective Board
- 03. Company Leadership
- 04. Productive Meetings
- 05. Ethical Culture
- 06. Board's Governance Roles and Conduct of Affairs
- 07. Insightful Strategy
- 08. Risk Management and Internal Controls
- 09. Board Committees
- 10. Receiving Assurance
- 11. Integrated Governance
- 12. Accountability to Shareholders
- 13. Stakeholder Engagement
- 14. Private Equity
- 15. Establishing a New Board
- 16. Managing Cybersecurity Risks
- 17. Corporate sustainability
- 18. Social media
- 19. Investment committees
- 20. Workplace safety & health
- 21. Appendices

### Insolvent and Fraudulent trading

Directors also have a duty to ensure that the company does not engage in insolvent trading. A company will be deemed insolvent if it is unable to pay its debts if and when they become due and payable<sup>29</sup>. Similarly, a director should not contract a debt where he, at the time of contracting, has no reasonable grounds of expecting the company to be able to pay<sup>30</sup>. The director will be personally liable for the payment of that debt.

Therefore, directors should constantly be on the lookout for signs that may suggest their company's financial reporting is misleading or disguising a serious deterioration in its financial stability. For example, irregular financial reporting, a lack of management focus on key financial ratios, insufficient maturity and liquidity analysis of the company's debt profile or lack of budgets or in-depth analysis of failure to meet budgets should all raise concerns for directors.

In addition, directors who knowingly consent to the company trading with the intent to defraud creditors will be personally liable for the debts incurred or could face fines up to S\$15,000 or imprisonment for a term up to 7 years, or both<sup>31</sup>.

### Maintenance of Capital

On matters relating to the company's capital, it is an imperative for directors to understand the Maintenance of Capital rule.

As a general rule, a company under Singapore law is required to maintain its capital in the sense that it cannot return capital to its members. This rule is intended to protect creditors.

Creditors of a company are said to give credit to the company on the faith that the capital of the company will be applied only for the purposes of the business and therefore have a right to insist that such capital be kept and not returned to the shareholders<sup>32</sup>.

However, due to the restrictive nature of the rule on a company's ability to alter its capital structure, this rule is now subject to many exceptions within the Companies Act. Therefore, depending on the Constitution of the company as well, a company may reduce its capital in the manner provided in the CA.

In certain specific transactions involving equity, a solvency statement is required to be made by directors. These include:

- Redemption of redeemable preference shares from capital<sup>33</sup>
- Giving of financial assistance by the company for the acquisition of its shares under s76(9A) or (9B)
- Reduction of capital under s78B or s78C

It should be noted that a director should have reasonable grounds to expect that the company is solvent, by conducting a careful assessment of the company's financial standing, before making a solvency statement. This is because a director that makes a solvency statement without having reasonable grounds for the opinions expressed in it will be guilty of an offence and shall be liable on conviction to a fine not exceeding S\$100,000 or to imprisonment for a term not exceeding 3 years or to both<sup>34</sup>.

29 CA Section 149(5)

30 CA Section 339(3)

31 CA Section 340(5)

32 <http://www.singaporelaw.sg/sqslaw/laws-of-singapore/commercial-law/chapter-16>

33 CA Section 70

34 CA Section 7A(6)

## Foreword

- **01. Directors' Legal Duties**
- 02. Structuring an Effective Board**
- 03. Company Leadership**
- 04. Productive Meetings**
- 05. Ethical Culture**
- 06. Board's Governance Roles and Conduct of Affairs**
- 07. Insightful Strategy**
- 08. Risk Management and Internal Controls**
- 09. Board Committees**
- 10. Receiving Assurance**
- 11. Integrated Governance**
- 12. Accountability to Shareholders**
- 13. Stakeholder Engagement**
- 14. Private Equity**
- 15. Establishing a New Board**
- 16. Managing Cybersecurity Risks**
- 17. Corporate sustainability**
- 18. Social media**
- 19. Investment committees**
- 20. Workplace safety & health**
- 21. Appendices**

### Dividends

Directors should also note that the company must not pay a dividend except out of profits<sup>35</sup>. A director who wilfully pays dividends in contravention with this rule is guilty of an offence and will be personally liable to creditors and the liquidator.

These problems are accentuated as corporate structures become more complex and parent companies become responsible for the affairs of numerous 'controlled entities'.

The concept of a controlled entity is not confined to a wholly or majority owned subsidiary. A company can be said to control another if it has the capacity to dominate the decision-making of the other entity, or to impose its interests on the other entity. Boards should seek professional advice if there is any doubt as to whether an entity is a 'controlled entity'.

### Continuous disclosure

Once a company is listed, it becomes subject to the jurisdiction of the SGX. Timely disclosure of price-sensitive information is the cornerstone of SGX's regulatory policy. To ensure that such information is released to the market on a timely basis, listed companies are obliged to comply with the rules relating to corporate disclosure in Chapter 7 of the SGX LR and SGX's Corporate Disclosure Policy in Appendix 7.1 of the of the SGX LR.

A listed company is required to keep its shareholders and the SGX informed of any material information relating to the group's activities or that could result in the establishment of a false market in its securities that might be price-sensitive<sup>36</sup>. Paragraph 8 of Appendix 7.1 provides

a non-exclusive list of matters which are considered to require immediate public announcement:

- A joint venture, merger or acquisition
- The declaration or omission of dividends or the determination of earnings
- Firm evidence of significant improvement or deterioration in near-term earnings prospects
- A sub-division of shares or stock dividends
- The acquisition or loss of a significant contract
- The purchase or sale of a significant asset
- A significant new product or discovery
- The public or private sale of a significant amount of additional securities
- A change in effective control or a significant change in management
- A call of securities for redemption
- The borrowing of a significant amount of funds
- Events of default under financing or sale agreements
- A significant litigation
- A significant change in capital investment plans
- A significant dispute or disputes with subcontractors, customers or suppliers, or with any parties
- A tender offer for another company's securities
- A valuation of real assets that has a significant impact on the financial position and/ or performance.

<sup>35</sup> CA Section 403

<sup>36</sup> SGX LR 703



## Foreword

### ► 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

The continuous disclosure requirements in the listing rules are given statutory backing by Section 203 of the SFA. Under this section, non-disclosure attracts both civil and criminal liability.

### Share trading

Subject to the general prohibition against insider trading, the SGX LR and the restrictions applying to directors under the share trading policy of a listed company, directors can in certain circumstances buy and sell shares and other securities in their companies.

SGX listed companies are required to have a share trading policy dealing in the company's securities by its directors and key management personnel. Under such policies, the directors and other key management personnel are restricted from trading in the company's securities during specified "prohibited periods" – typically for a period before the release of financial results and/or only permitted to trade during certain defined "trading windows".

An issuer is required to disclose if and how they comply with the following best practice of dealing in securities<sup>37</sup>:

- By devising and adopting its own internal compliance code to provide guidance to its officers with regard to dealing by the listed issuer and its officer in its securities
- An officer should not deal in his company's securities on short-term considerations
- A listed issuer and its officers should not deal in the listed issuer's securities during the period commencing two weeks before the announcement of the company financial statements for each of the first three quarters of its financial year and one month before the announcement of the company's

full year financial statements (if required to announce quarterly financial statements), or one month before the announcement of the company's half year and full year financial statements (if not required to announce quarterly financial statements).

### Other Legal Obligations

Directors are also subject to other statutes, including:

- Tax – answerable to acts and matters as required to be done under the Singapore Income Tax Act (Chapter 134) for the assessment of the company and payment of tax (Section 55 of the Income Tax Act)
- Employment – where an offence under the Singapore Workplace Safety and Health Act (Chapter 354A) has been committed by an officer (defined to include director), the person will be liable to be proceeded against and punished accordingly
- Environment – a director will be liable and punished under Section 71 of the Environmental Protection and Management Act if found guilty of an offence under this Act
- Industry specific – for example, the Singapore Banking Act (Chapter 19) and the Singapore Insurance Act (Chapter 142) impose additional duties on directors of companies regulated under these statutes.

### Director Liabilities

Directors have considerable responsibilities and liabilities. A breach of duties by a director is an offence under the CA and could result in a civil suit under common law or criminal liabilities and prosecutions under statutory duties. In certain circumstances, the Court may make an order to disqualify the person from being a director.

37 SGX LR 1207(19)(b)

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

In addition, the SGX LR 720(2) would require a director to resign from the Board immediately after being disqualified from acting as a director in any jurisdiction for reasons other than on technical grounds. Some of the significant and common breaches are detailed below:

| Offence  | Effect   |
|--|--|
| Any other breach of trust e.g. theft, misappropriation of property, non-payment of employees' wages, etc.                      | Subject to criminal prosecution  |
| S157(1) & (2) Duty to act honestly and with reasonable diligence and Duty not to make improper use of position and information | Fine not exceeding \$5,000 or imprisonment for a term not exceeding 1 year <sup>39</sup>   |
| S165(1) Duty to disclose interests that directors have in the company  | Fine not exceeding \$15,000 or imprisonment for a term not exceeding 3 years; further fine of \$1,000 for every day offence continues after conviction |
| 156(1) & (5) Duty to disclose potential conflicts of interests in transactions or ownership or property                        | Fine not exceeding \$5,000 or imprisonment for a term not exceeding 1 year <sup>40</sup>   |
| 199(1) Duty to keep proper accounts  | Fine not exceeding \$2,000 or imprisonment not exceeding 3 months and also subject to a default penalty  |
| SFA Section 218, Chapter 289 Insider dealing offence   | Fine not exceeding \$250,000 or imprisonment for a term not exceeding 7 years or both.   |

38 CA Section 157(3)(b)

39 CA Section 156(10)

Civil suits have also resulted in the following liabilities for the directors:

- Pay compensation for losses - Chew Kong Huat v Ricwil [2000] 1 SLR 385
- Forfeit any commissions received - Andrews v Ramsay[1903] 2 KB 635
- Avoid contracts director signed - Lim Koei Ing v Pan Asia Shipyard [1995] 1 SLR 499
- Personally liable for debts if company's business was carried out with intent to defraud - Rahj Kamal v PP [1998] 1 SLR 447.

## Foreword

- 01. Directors' Legal Duties
- 02. Structuring an Effective Board
- 03. Company Leadership
- 04. Productive Meetings
- 05. Ethical Culture
- 06. Board's Governance Roles and Conduct of Affairs
- 07. Insightful Strategy
- 08. Risk Management and Internal Controls
- 09. Board Committees
- 10. Receiving Assurance
- 11. Integrated Governance
- 12. Accountability to Shareholders
- 13. Stakeholder Engagement
- 14. Private Equity
- 15. Establishing a New Board
- 16. Managing Cybersecurity Risks
- 17. Corporate sustainability
- 18. Social media
- 19. Investment committees
- 20. Workplace safety & health
- 21. Appendices

### Directors' indemnities and insurance

A company cannot by provisions of the Constitution or any other contract exempt a director from or indemnify the director against, any liability in respect of any negligence, default, breach of duty or trust which by law he may be guilty of<sup>40</sup>.

However, the company is allowed to purchase and maintain insurance for any officer (including a director) against any liability in relation to discharging duties as a director and may indemnify directors against any legal proceedings incurred provided the judgement is in favour of the director or in which the director is acquitted<sup>41</sup>.

In addition, the Constitution of a Singapore company would generally contain an indemnity provision for the company's directors to be indemnified against any liability incurred in relation to the discharge of duties as a director. The terms of the Constitution may be incorporated into an agreement between the company and each director since the Constitution does not constitute a contract.

A surge in the number of legal actions against directors, particularly those brought by Singapore's regulatory authorities in recent years has led to a gradual shift for companies in Singapore to purchase directors' and officers' insurance (D&O insurance). Directors must also understand their potential personal liabilities, and the extent to which they can be indemnified for liabilities through the D&O insurance because, they cannot assume full protection even in cases where D&O insurance cover is purchased. Where there are circumstances in which directors are accused of wrongdoing by his or her company, the company may not activate the D&O insurance policy. More common sources of claims are where one director is being sued by another director, both of whom are Board members of the same company; in such a case, the D&O insurance purchased by the company would not take effect. As a result of this, directors may consider purchasing personal D&O insurance policy exclusively for their own individual protection.

40 CA Section 172

41 CA Section 172A

## Foreword

### 01. Directors' Legal Duties

### ► 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

# 2. Structuring an Effective Board

The structure, composition and internal dynamics of Boards can affect the performance of individual directors and the Board as a whole.

## Questions that company Directors should ask

- |  |   |
|--|---|
| 1. Is the Board clear on the criteria to be applied for the recruitment of the next director?                        | 7. Does the Board, collectively, possess a wide range of competencies and experience to effectively deal with the opportunities and issues the company faces? |
| 2. Is a tailored competency and behavioural-based analysis undertaken prior to selecting new directors?              | 8. Is there an appropriate mix of skills, backgrounds, experience, age, gender and perspectives on the Board?   |
| 3. Are there any significant conflict of interest issues that could make it difficult to accept a Board appointment? | 9. Do all new directors receive a letter of appointment setting out key terms and conditions?   |
| 4. Do you believe you can work cooperatively and constructively with existing directors?                             | 10. Is there an appropriate induction program (including committee induction) for new directors and continuous training for all directors?                    |
| 5. Does the Board have a robust process for handling succession planning?  | 11. Does the Board regularly review its own performance and the effectiveness of its governance process?  |
| 6. Is a contingency plan established in the event that the Chairman has to step down unexpectedly?                   |   |

## Red flags

- |   |  |
|---|--|
| ► Board appointments are decided by the Chairman with little input from other directors | meeting to the next  |
| ► Board discussions are dominated by one or two directors                               | ► The Board does not periodically review its skills and competencies           |
| ► Unreasonable demands are placed on the directors' time                                | ► Gaps identified in Board assessments are not actioned in a timely manner     |
| ► The Board is too large or too small as compared to similar organisations              | ► There is a lack of ongoing Board succession planning                         |
| ► Overuse of external advisers occurs due to skill gaps on the Board                    | ► No formal (or insufficient) Board induction is provided to new Board members |
|   | ► No regular training or developmental programs conducted for all directors    |
| ► There is consistent carry-over of agenda items from one                               |  |



## Foreword

### 01. Directors' Legal Duties

### ► 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

### Governance structure

It is imperative for companies to consider adopting a process for the search, selection, nomination and appointment of directors to the Board so that the company is headed by an effective Board to lead and control the company for the long-term success of the company<sup>42</sup>. There needs to be a formal and transparent process for the appointment and re-appointment of the Board members<sup>43</sup>.

A well designed governance structure will help Boards to function effectively by:

- Clarifying Board appointments with defined terms of reference for each director and Board committees
- Improving the balance of skills and expertise of the Board and Board committees in ensuring that the company's current and long term strategies are fulfilled
- Enhancing communications amongst the Board members, management and shareholders
- Instilling confidence in shareholders and the public that the company is well governed

The Board should establish the maximum number of directorships that a director may hold and disclose this in its annual report to ascertain whether a director has the ability to devote adequate time for his roles and responsibilities<sup>44</sup>.

### Skills and expertise

The Board should be made up of a group of professionals with the right mix of skill sets and expertise that complement each other. The various disciplines and backgrounds will enable the Board to function more

effectively as a whole and make good decisions when it has core competencies in business, operational planning and management, accounting and finance, risk management, strategy, legal, other industry-related expertise and independence. The competencies required for any particular Board will vary considerably, depending on industry, strategy and business environment.

The NC should review the performance of the Board members which should include assessment in terms of individual director's competencies and whether each director continues to contribute effectively and demonstrate commitment to the role<sup>45</sup>. The NC should also discuss professional development needs and programs for directors particularly on relevant new laws, regulations and changing commercial risks, from time to time.

In addition to a competency assessment, an analysis of director behavioural types may help the Board function as an effective decision-making body. When selecting future directors and planning director education, a tailored competency and behavioural-based analysis may assist the Board to identify gaps and focus on recruiting individuals with the required competencies.

Key information regarding each director's academic and professional qualifications should be disclosed in the company's annual report<sup>46</sup>.

### Boardroom diversity

In structuring an effective Board, the company must consider diversity of its Board members based on mix of skills, backgrounds, experience, expertise, age, gender and perspectives of its directors that would be necessary to meet the unique requirements of the company.

42 CG Code Principle 1

43 CG Code Principle 4

44 CG Code Guideline 4.4

45 CG Code Guideline 1.6 & 5.3

46 CG Code Guideline 4.7

## Foreword

### 01. Directors' Legal Duties

### ► 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

The NC, usually led by the Chairman, should be responsible for Board recruitment with the objective of securing a boardroom which achieves the right balance between challenge and teamwork, fresh input and thinking, while maintaining a cohesive Board. It is also important to consider a diversity of personal attributes among Board candidates, including intellect, critical assessment and judgement, courage, openness, honesty and tact, the ability to listen, forge relationships and develop trust, diversity of psychological type, background and gender to ensure that a Board is not composed solely of like-minded individuals. There may be a blind spot if Board members consist of people who read the same books, move in the same circles and exchange similar views.

Diversity is an important factor in order to have effective and high-performing Boards. The ideal is to have Boards of appropriate composition, size, diversity of skills, experience, gender and knowledge of the company. In addition, they should also possess core competencies such as accounting and finance, business or management experience, industry knowledge, strategic planning and customer-based experience<sup>47</sup>.

The Organisation of Economic Board Co-operation and Development (OECD) recommend the following for Boards to improve their composition and effectiveness by:

- Considering a wider set of skills and experience for directors, in particular financial industry experience, risk management and remuneration expertise
- Emphasising Chairman's leadership skills and industry experience

- Enhancing director search and nomination process
- Placing importance on having a robust process in determining independence of directors
- Improving the process of assessing gaps within the Board, Board committees, Chairman and individual directors
- Improving the Board evaluation process by using a qualified external party as facilitator
- Improving time commitment of directors

A report by Diversity Action Committee Singapore in February 2016 released interesting findings about female representation at the Board level of SGX Listed Companies. Gender diversity remains a challenge in Singapore's Boards. However, women's representation on Boards of companies listed on the SGX rose more rapidly in 2015. As at end 2015, women held 9.5% of the 5,029 directorships (Board seats) on SGX listed companies, up from 8.8% at end 2014. Of the women appointments in 2015, 38% were first time directors. The number of all-male Boards continued to decline across companies of all sizes in 2015. Straits Times Index (STI) companies showed the most significant decline of 30% from the previous year. There remained only 9 of the 30 STI companies who do not have women on Boards. Singapore, like other financial markets, is working towards increasing women's representation on Boards. SGX-listed company Boards are gaining ground despite not having quotas or mandatory disclosure obligations.

As for now, the NC should be an effective and efficient mechanism for the independent selection, examination and appointment of directors to the Board. It is therefore the Board's responsibility to strengthen the effectiveness of the Board in decision-making by achieving the right balance in terms of size and diversity.

47 CG Code Guideline 2.6

## Foreword

### 01. Directors' Legal Duties

### ► 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

### Board size

The Board is required to examine its size to enable it to function effectively and facilitate effective decision making, having regard to the scope and nature of the operations of the company, the requirements of the business and the need to avoid undue disruptions from changes to the composition of the Board and Board committees<sup>48</sup>.

The size of the Board will vary depending on the type of business, industry, size and complexities of the company's business and its operating environment, range of competencies, mix of executive and non-executive directors, and number and nature of Board committees. In addition, the company's Constitution may limit the size of the Board and any amendment to this limitation may require shareholders' approval in a general meeting.

### Finding and appointing new directors

Appointing new directors who are able to make a positive contribution is one of the key elements of Board effectiveness. The NC should evaluate the existing and future Board composition requirements to identify where there is a gap in terms of having the appropriate age group, gender, qualifications, experience, personal attributes, public office, community standing and skills. Potential new members can be recommended by existing fellow Board members, business associates or by engaging a professional search firm to identify potential candidates. The outcome of this process will be a brief containing detailed selection criteria approved by the Board.

There should be a robust and transparent process to Board appointments and succession planning

48 CG Code Guideline 2.5

development<sup>49</sup>. A description of the process for the selection, appointment and re-appointment of directors to the Board should be disclosed in the company's annual report. This should include disclosure on the search and nomination process.

The NC should personally meet with the candidates to assess suitability and to support selection. Evaluation criteria includes qualifications, business and related experience, commitment, ability to contribute to the Board process and if the potential candidate will be able to fulfil the Board's existing need for such a new member. Upon completion of its assessment, the NC should recommend the nomination of successful candidates to the Board.

Directors are normally appointed by a resolution passed at a general meeting of the company.

The CA does not impose educational or specific qualifications for appointing directors. However, the following circumstances will not qualify someone to hold office as a director and also contributes to the disqualification of an existing director:

- Anyone who is an undischarged bankrupt<sup>50</sup>
- Anyone who is automatically disqualified for up to 5 years if convicted of an offence involving fraud or dishonesty<sup>51</sup>
- Anyone who has a disqualification order made against him by a court
- Anyone who has 3 or more High Court Orders made against him compelling compliance with the relevant

49 CG Code Principle 4

50 CA Section 148

51 CA Section 154(1)

## Foreword

### 01. Directors' Legal Duties

### ► 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

requirements of the Act within a period of 5 years

- Anyone convicted of 3 or more offences relating to filing requirements under the Act within a period of 5 years<sup>52</sup>
- Anyone who is a director of an insolvent company<sup>53</sup>
- Anyone who was a director of a company which was wound up on the grounds that it is being used for purposes against national security or interest.<sup>54</sup>

### Director due diligence

The role of a director has become significantly onerous over the years with more demanding responsibilities and liabilities. A prospective director should carry out sufficient due diligence prior to accepting the appointment. The individual needs to:

- Understand company's business, finance and other disciplines relevant to the success of a public-listed company
- Review documentation provided by the company including policies and strategy and access to resources that the company lacks
- Review financial data, announcements made by SGX-ST in the last 12 months, press releases
- Assess personal commitment to contributing and devoting time to the long-term interest of the company and willingness to sit on or chair such sub-committees of the Board as may be required from

time to time. The individual should pay attention to competing time commitments with his or her multiple

<sup>52</sup> CA Section 155

<sup>53</sup> CA Section 149

<sup>54</sup> CA Section 149A

Board representations. In addition, the director should enquire the company's policy on the maximum number of directorships which any director may hold<sup>55</sup>

- Ascertain any potential diverging interests that could create conflict of interest situations
- Assess information regarding the company's leadership and management; arrangements to speak with other key directors, senior management executives be made. Consider if the company has a culture of candour, transparency and voluntary disclosure
- Ascertain if there is any current litigation and potential liability of the company by meeting its external and internal legal counsels and auditors
- Ascertain if there has been any queries from regulatory authorities
- Adequacy of director's D&O and remuneration package.

### Director letter of appointment

The new director should be issued with a letter of appointment<sup>56</sup>, setting out the terms and conditions of appointment, including:

- Period of office
- Compensation and benefits
- Duties and responsibilities
- Resignation and termination.

<sup>55</sup> CG Code Guideline 4.4

<sup>56</sup> CG Code Guideline 1.7

## Foreword

### 01. Directors' Legal Duties

### ► 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

### Director induction and education programs

Directors bring to their Boards a wealth of experience, knowledge and skills generated over their careers. Boards should nevertheless design and implement an effective orientation program for new directors and should encourage and finance continuing education.

Director induction programs are designed to make the most of a director's existing knowledge base by filling any knowledge gaps, typically concerning the company's industry, the competition landscape and technical issues, as well as familiarising the director with all aspects of the company. Induction programs make it more likely that new directors can make an immediate contribution.

There is no prescriptive formula for what should be included in an induction program. The elements of the program should be tailored to take account of the appointee's knowledge and experience, and will vary depending on company structure, processes and the major issues it faces.

Typically, a combination of written materials, coupled with presentations and activities, such as meetings and site visits, will provide the appointee with a realistic picture of the company's position and the challenges it faces. It will also serve to foster a constructive relationship between the new director and their fellow directors and senior management.

The Chairman should take a leading role in ensuring the delivery of a tailored and properly balanced induction program, which is facilitated by the Company Secretary. Initially, a new director should receive an induction pack, which may include the following:

- Corporate information – strategic and business plans, financial accounts, regulatory frameworks, major shareholders, corporate communications, overview of the company's competitors and industry information, risk profile and appetite, company history and product information
- Governance framework – Board charter/ governance statement, annual agenda, selected Board packs, full details of directors, committee structures, Board process, assurance providers, resources available, key stakeholders, procedures for sign-off of financial statements and items requiring approval outside of Board meetings
- Management information – names and background of senior management, organisational and management structure outline etc.

In addition to the provision of induction materials, it is also important to schedule in-depth meetings for the new director to discuss the Board's charter, how the company operates, main business issues, the financial position, business value drivers, and other matters of significance.

An induction to Board committees, with particular emphasis on those Board committees which the new director will join, should not be overlooked. An induction pack containing relevant documents such as committee charters, annual agendas, copies of minutes, plus a full briefing by the relevant committee Chairman will help the new director gain an appreciation of the major issues.

The NC should recommend to the Board the training and professional development programmes for the Board<sup>57</sup>.



## Foreword

### 01. Directors' Legal Duties

### ► 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

Through the Board evaluation process, areas will be identified where further education may enhance Board and individual director effectiveness. The Board should ensure that resources are budgeted to provide appropriate educational opportunities for directors. The Chairman should address the development needs of the Board as a whole, plus those of individual directors, with the Company Secretary playing a key role in facilitating the process.

### Board evaluation

Board evaluations enable the effectiveness of a Board to be assessed in relation to:

- fostering communications amongst directors, management and other stakeholders
- coordinating efforts of the Board as a whole and utilising the company's resources to achieve the company's long term goals.

It is a tool for the Board's continuous improvement and learning. The process also identifies the "best fit" in Board composition with the objective of improving shareholders' value over time.

There should be a formal annual Board evaluation process (to be disclosed in the company's annual report) as a whole, for Board committees and the individual director<sup>58</sup>.

### What are the criteria to include for Board evaluation?

Relevant performance criteria to be considered as recommended by the Statement of Good Practice SGP No.8/2008 could comprise the following:

- Company-related factors
  - company's share price performance over a five-year period vis-à-vis the Singapore Straits Times Index
  - a benchmark index of its industry peers return on assets, return on equity, return on investment and economic value added over a longer-term period
- Director-related factors - contribution and commitment to the role, attendance at meetings, involvement and actual participation at meetings, additional responsibilities assigned to the relevant directors, including involvement in sub-committees of the Board.

Board effectiveness assessment should cover key areas:

- Board culture and dynamics
- Board composition and role of Board leaders
- Board organisation, processes and procedures
- Quality of information (written and verbal) and accessibility provided during Board meetings
- Board's relationship with senior management
- Potential Board developmental needs
- Shareholders' engagement and communications.

The NC is responsible for design of the evaluation process (but many engage an external party to assist). Companies adopt various techniques in conducting Board assessment i.e. some companies evaluate the performance of its Board through analysing results completed by individual directors in the form of a questionnaire whilst others may engage an external party to conduct interviews.

58 CG Code Principle 5

## Foreword

### 01. Directors' Legal Duties

### ► 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

Board assessment will provide highest value when the following factors exist:

- ***The objective of the evaluation is clear***

Boards must agree to the purpose and process of the evaluation. Questions or roadblocks to effectiveness have to be addressed at the onset. To be effective, the evaluation process must be relevant to the company's Board and governance structure and cultural norms.

- ***A Board leader drives the process***

The Board performance evaluation is carried out by the NC with a clear process articulated and recommendations identified for approval by the entire Board<sup>59</sup>. The performance criteria should be comparable with other industry peers and should address how long term shareholder value can be enhanced<sup>60</sup>. The evaluation technique should be reviewed periodically to ensure that gaps are identified in order to make the process more productive.

- ***The process incorporates perspectives beyond the Board directors themselves, including those from senior management and best practices from outside the company***

Constructive feedback can come from senior management e.g. CFOs, CEO, legal counsel, HR who interact with the Board regularly. The Board assessment can also be more valuable when it is being benchmarked against other high performing Boards in the same industry or against leading practices for a specific area. A third-party facilitator with significant experience in the boardroom and knowledge of governance guidelines and regulations can provide

perspectives on how the Board compares to its peers or how it "measures up" to the evolving standards of corporate governance by providing an up-to-date perspective on leading practices.

- ***The assessment process goes beyond compliance issues to examine Board effectiveness across a broad range of measures***

The NC together with the Board should consider if the evaluation should be done internally by another committee, by the NC, by self-evaluation or by an external consultant. The NC should also determine whether the process is intended to be conducted through a written questionnaire, or via interview or a combination of both.

In most effective Board assessments, directors are interviewed individually on a confidential basis and asked for both their qualitative and quantitative assessment of the key areas that determine the effectiveness of the Board. Studies suggest that the most effective way of conducting the evaluation is via individual confidential interviews and review of governance documents, committee charters, Board meeting minutes, Board meeting agendas and observation of a live Board meeting in determining the quality of discussions and interactions between members. Boards many also consider discussing areas such as succession planning and strategy planning for early involvement. Such interviews and assessments should be facilitated by an experienced boardroom person or consultant who understands boardroom issues and CEO/Board relations. This person has

<sup>59</sup> CG Code Principle 5.1

<sup>60</sup> CG Code Principle 5.2

## Foreword

### 01. Directors' Legal Duties

### ► 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

to be in a solid position to discuss a wide-range of topics - Board composition, Board processes, roles and responsibilities to communication, boardroom dynamics, the Board/ management relationship and the quality of boardroom discussion. *[The Executive Guide, Improving Board Effectiveness Five Principles for Getting The Most out of a Board assessment, 2012].*

Directors must commit to reviewing the results of the assessment together and address issues that emerge on a timely basis.

The Board should not treat the assessment as part of a compliance exercise i.e. where the process is initiated, with no concerted effort and commitment made in reviewing the results of the evaluations on a timely basis. Boards need to be open and receptive of the results and deal with the findings appropriately and timely. Clear action plans and timelines to address the gaps identified need to be established by the Board. A committee may be set up to monitor the progress and/ or oversight future follow up assessments. In addition, the Board, along with the NC Chairman, should take appropriate steps to counsel or, at worst, replace non-performing directors.

- Board evaluation should be kept confidential throughout the process
- Board appreciates the benefits of evaluations.

Effective Board, Board committee and individual director evaluations improve:

- Effectiveness by identifying gaps, if any, and correcting them
- Focus on how it operates and identifies areas that can be enhanced

- Focus on long-term strategies
- Credibility in having a written record to show that the Board is focused on continuous improvement and diligent in monitoring its own actions.

However, directors need to take note that written records of the Board evaluation process may be relied upon in litigation. Any areas identified as gaps which have not been actioned could possibly be used adversely during the litigation.

### Director remuneration

Directors' remuneration is a sensitive discussion matter to be deliberated by the Board. The power to remunerate directors is also provided in the Company's Constitution.

There should be a clear policy and procedure in developing remuneration for executives and independent directors. Directors' remuneration has to be aligned with the long term objectives and risk management policies of the company. It should also be structured so as to link rewards to corporate and individual performance<sup>61</sup>. There needs to be a balance between attracting and retaining directors with the appropriate skills and the fees paid to them for discharging their duties properly based on the size and complexity of the Company's operations<sup>62</sup>.

The executive directors' and key management remuneration should be linked with the interests of the shareholders i.e. performance of the company as a whole and as individuals. Long-term incentives such as shares or grants of options where only a portion of the benefits can be exercised each year is encouraged in Singapore<sup>63</sup>.

<sup>61</sup> CG Code Guideline 8.1

<sup>62</sup> CG Code Principle 8

<sup>63</sup> CG Code Guideline 8.2

## Foreword

### 01. Directors' Legal Duties

### ► 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

Similarly, non-executive directors should be remunerated appropriately according to the level of contribution and responsibilities; aligned with the interests of the shareholders and in this case a consideration is to offer share schemes. However, non-executive directors should not be over-compensated to the extent that their independence is impaired<sup>64</sup>.

Larger organisations will often develop a fee system that compensates directors according to the number of subcommittees in which they participate, and whether they participate as the Chairman or member. Some further issues to take into account when setting fees are the company's current policy with regard to Board fees, the experience and knowledge of the potential directors in comparative companies (of size and industry) and the size and complexity of the business.

The remuneration scheme should be annually reviewed based on the individual's responsibilities and performance, and can include a peer group benchmarking, if warranted.

SGX LR 1207(12) requires an issuer to make disclosure on directors' and key executives' remuneration as recommended in the Code. Full disclosure of the remuneration of each individual director and the CEO on a named basis<sup>65</sup> should be provided in the annual report<sup>66</sup>. The issuer should also name and disclose the remuneration of at least the top five key management personnel (who are not directors or the CEO) in bands of S\$250,000<sup>67</sup>. There should be a breakdown of each director's and key executive's remuneration earned through base salary, variable or performance related income/ bonuses, benefits in kind, stock options, share-

64 CG Code Guideline 8.3  
65 CG Code Guideline 9.2  
66 CG Code Guideline 9.1  
67 CG Code Guideline 9.3

based incentives and other long term awards<sup>68</sup>. For transparency, the annual remuneration report should disclose the details of the remuneration and relationship of employees who are immediate family members of a director or the CEO, and whose remuneration exceeds S\$50,000 during the year<sup>69</sup> as well as the link between remuneration paid to the executive directors and key management personnel, and performance<sup>70</sup>. The annual remuneration report should also contain details of employee share schemes to enable their shareholders to assess the benefits and potential cost to the companies<sup>71</sup>.

## Board succession planning

Board succession planning challenges Boards to anticipate and plan for their future needs. Such an important and on-going exercise is led by the NC. It should be a continuous process that is regularly reviewed by the Board so that changes in the Board composition can be anticipated and planned for in advance. A strategic map of succession planning should be in place, initiating the plan from 12-24 months.

Board succession planning is built on:

- An assessment of the challenges and opportunities facing the company, both current and in the future
- An analysis of the core skills, competencies and behaviours that are required, both immediately and in the future
- An evaluation of the skills, competencies and behaviours of existing directors, including their strengths and weaknesses, skills and experience gaps, current age, gender composition and length of tenure
- Assessments of existing directors' performance.

68 CG Code Guideline 9.2 & 9.3  
69 CG Code Guideline 9.4  
70 CG Code Guideline 9.6  
71 CG Code Guideline 9.5

## Foreword

### 01. Directors' Legal Duties

### ► 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

In developing a succession plan, the Chairman's role needs to be considered. In situations where the current Chairman's retirement period is known, plans can be drawn up to identify a new Chairman, either internally or externally. Companies should also have a contingency plan for the Chairman's role, in the case of some unexpected event.

The recent repeal of Section 153 of the Companies Act, which limited the age of directors to 70 years, could place more attention on succession planning and Board renewal. Whilst this section imposed a mandatory retirement age for directors, Boards will now have to give more consideration to whether a director continues to remain fit in both mind and body, and is still able to make a valuable contribution to the Board.

The optimal Board composition should be reviewed by the Chairman with the assistance of the NC to review the skills required, identify the gaps, develop transparent appointment criteria and address succession planning. Executive directors may be recruited from external sources, but companies should also establish a framework to develop internal talent capabilities. Initiatives might include middle management development programmes, facilitating engagement from time to time with non-executive directors, partnering and mentoring schemes.

A survey of all SGX-listed companies (743) based on the 2010 data undertaken by the NUS Business School Centre for Governance, Institutions and Organisations in 2012 revealed that family firms are the dominant type of organisations (with 52%) among Singapore listed companies and on average, 35% of the Board of a family firm consists of family members. Having established this fact, succession planning for a CEO is crucial as the impact on this type of company is high. Employees are sometimes loyal to the family leader and not the hired CEO outside the family circle.

Hiring an outside CEO may have negative implications i.e. the person may not be able to garner the professional support that he used to get or was able to develop from past experiences. In addition, the family members who are on the Board or holding key management positions may undermine the authorities of the outside CEO. Therefore, ownership and management has to be carefully considered when considering succession planning in listed companies previously owned and currently led by family members, without compromising the proper governance of the company by its Board.



## Foreword

01. Directors' Legal Duties
- 02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices



## Case Study



Due to public outrage and pressure for management accountability over two major breakdowns in train services, Ms. Saw Phaik Hwa, SMRT's then CEO resigned on 6th January 2012. Following her resignation, SMRT's independent director, Mr. Tan Ek Kia, had assumed the role of interim CEO while the Board searched for a new CEO. Ms. Catherine Lee, the CFO of SMRT made a statement stating that although the search for a new CEO had begun, "it will take some time". Eventually, Mr. Desmond Kuek took over the role of CEO on 1st October 2012.

In this case, the resignation of Ms. Saw, although abrupt and against her insistence on staying in the job, came after mounting public anger, and brought to light the room for improvement in SMRT's succession planning<sup>72</sup>.

<sup>72</sup> <https://sg.news.yahoo.com/smart-ceo-saw-phaik-hwa-resigns.html>

## Foreword

### 01. Directors' Legal Duties

### ► 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

### Access to company records

Directors should have access to complete, adequate and timely company information at all times so as to enable them to make informed decisions in discharging their duties<sup>73</sup>. Directors are entitled to request from management additional information as needed to make informed decisions and the management shall provide required information in a timely manner<sup>74</sup>.

Information that management should furnish the directors includes timely Board papers and related materials, disclosure documents, budgets, periodic financial statements with fluctuations in the budgeted and actual results being adequately and satisfactorily explained<sup>75</sup>. Such information should be furnished to the Board monthly or/as and when required for the Board to make balanced and informed decisions<sup>76</sup>.

It is generally established practice for:

- directors not to retain individual copies of Board papers
- a deed of access between the company and each director to be executed.

The Board could consider adopting an information policy which provides that the Company Secretary holds a complete set of Board and committee papers. Under this policy, directors should be entitled, on request, to access Board papers for the period during which they were a director, even if they have ceased to be a director. Increasingly, such papers are being held electronically, with approval granted to directors, enabling easy access and avoiding the need for the retention of papers by individual directors.

73 CG Code Principle 6  
74 CG Code Guideline 6.1 & 6.2  
75 CG Code Guideline 6.2  
76 CG Code Guideline 10.3

### Director resignation, retirement and removal

A director may resign by giving notice in writing to the company, unless the company's Constitution provides otherwise.

A director is not allowed to resign or vacate his office (notwithstanding the provisions in the company's Constitution or any agreement with his company) unless there is remaining in the company at least one director who is ordinarily resident in Singapore<sup>77</sup>. The company's Constitution would provide the various situations in which a director may vacate the office. A public company may by ordinary resolution remove a director before the expiration of his period of office, notwithstanding anything in its Constitution or in any agreement between it and him but where any director so removed was appointed to represent the interests of any particular class of shareholders or debenture holders the resolution to remove him shall not take effect until his successor has been appointed<sup>78</sup>.

All directors should be required to undergo a renomination process and be re-appointed at regular intervals and at least once every three years<sup>79</sup>. The independence of the directors will need to be examined if they have served on the Board beyond nine years<sup>80</sup>.

The resignation or removal of directors may have negative consequences if not handled with care as resignation of one director or a succession of them, particularly of independent directors, may indicate something untoward in terms of corporate governance or commercial developments.

Directors resigning should complete the announcement template on SGXNET for notice of resignation and provide clear, adequate reasons for resigning<sup>81</sup>. Any director's resignation has to be announced immediately<sup>82</sup>.

77 CA Section 145(5)  
78 CA Section 152(1)  
79 CG Code Guideline 4.2  
80 CG Code Guideline 2.4  
81 SGX LR 704.7)  
82 SGX LR 704(7)

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
- ▶ 03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

# 3. Company Leadership

Most Boards would agree that one of their most important governance roles is hiring and possibly firing the CEO. After all, the CEO is responsible for the day-to-day operations of the organisation and is instrumental in the development of corporate strategy.

## Questions that company Directors should ask

- |  |  |
|--|--|
| 1. Does the Board have complete confidence in the CEO and the senior management team?  | 6. Is the CEO's view regarding senior management team members and other talented people with strong leadership qualities considered? |
| 2. Does the CEO encourage the development of talented people?  | 7. Has the Board developed a CEO and senior management succession plan that is periodically reviewed?                                |
| 3. Does the CEO, through attitude and behaviour, reinforce the appropriate 'tone at the top'?  | 8. Do the CEO's responsibilities include attracting, developing and retaining high performers in the organisation?                   |
| 4. Does the Board have in place a robust CEO selection process, using an external search firm to identify suitable internal and external candidates? | 9. Are concerns about the CEO's performance discussed with the CEO and appropriately documented?                                     |
| 5. Prior to the appointment of a new CEO, does the Board (through the Chairman or Nominating Committee), conduct rigorous reference checks?          | 10. Does the Board have a transparent process for determining management remuneration?   |

## Red flags

- |  |  |
|--|--|
| ▶ The CEO selection process was conducted largely in-house within a pool of Board members' friends and business associates | ▶ CEO performance appraisal is conducted infrequently and informally within a pool of Board members' friends and business associates |
| ▶ Support and confidence in the CEO is divided amongst Board members   | ▶ No contingency plan or succession plan exists for the current leadership structure   |
| ▶ The CEO does not have KPIs or they are often not being met   | ▶ The CEO seems focused mostly on achieving his own remuneration targets   |
| ▶ Remuneration setting is discussed mostly privately   |  |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
- ▶ 03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### CEO and executive management

The CEO is involved in nearly all Board decisions, wields considerable delegated authority, reinforces the 'tone' of the enterprise and represents the organisation to external parties.

It is usual practice for a CEO to establish an executive management team (or similar) to assist in the management of the day-to-day activities of the organisation and to assist with strategy development and execution. The executive management team's typical functions include:

- Supporting the CEO
- Exchanging information and ideas
- Providing input on the organisation's direction
- Influencing the organisation at all levels.

Building a strong executive management team is essential for organisational success. Factors associated with strong organisational leadership include:

- Respective Board and management roles and responsibilities clearly delineated and articulated in writing
- Board protocols covering directors' access to executive managers outside of Board meetings
- A CEO that provides appropriate direction, mentoring, support and guidance to executive management team members
- Executive management team members who are empowered to share leadership responsibilities
- Executive management team members who are rewarded for organisational, business unit and individual performance, based on behavioural standards displayed and value creation outcomes
- Management succession and development plans

that cover all key positions, based on competencies, behaviours and experience to achieve the strategic vision

- Full disclosure of conflicts of interest.

**"Leaders establish the vision for the future and set the strategy for getting there: they cause change. They motivate and inspire others to go in the right direction and they, along with everyone else, sacrifice to get there."**

Dr John Kotter, Konosuke Matsushita Professor of Leadership, Emeritus (Harvard Business School)

### Role of the CEO

It goes without saying that, as a company's most senior officer, the CEO is critical to the performance of the enterprise. The scope of activities and responsibilities assigned to the CEO are broad and far-reaching. Through their attitudes and behaviours, CEOs are instrumental in reinforcing the 'tone' of their organisations.

An effective CEO:

- Passionately leads and develops people
- Is wise, courageous and makes the tough decisions
- Always acts with integrity
- Drives strategic vision and innovation
- Is resilient in the face of setbacks
- Successfully adapts to the company's ever-changing circumstances
- Demonstrates high-level business acumen
- Meets immediate performance targets without neglecting longer-term growth opportunities.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
- ▶ 03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

The titles CEO and managing director (MD) are often used interchangeably. In theory, a CEO does not necessarily have a seat on the company's Board, whilst the MD is, by definition, a director. CEOs of listed Singaporean companies often occupy a seat on the Board.

In putting its relationship with the CEO on a sound footing, a Board needs to formulate a CEO's job description and define the criteria for the CEO's performance-based remuneration. There should also be a formal statement delineating the boundaries between Board and management responsibilities, including the Board's retained authorities and those delegated to management (which is usually set out in the Board charter). A high-performing Board will invest time and effort in constructing a synergistic partnership with the CEO and senior management. It will not be a relationship based mainly on supervision, but one in which the Board engages with the CEO and senior management to achieve outstanding results.

### *CEO succession planning*

The purpose of succession planning is to ensure the Board always has available a number of successor candidates in the event that the incumbent CEO departs suddenly and unexpectedly. Ideally, succession planning should start from day one of a new CEO's appointment. Each company's needs are unique and change over time, as does the available pool of talent from which a new CEO may be drawn. The Board should ask the CEO to provide an assessment of the key internal contenders and what is being done to develop their strengths and to overcome any limitations.

Some companies approach succession planning by considering different contingencies, ranging from crisis management (e.g. if the CEO got hit by a bus, could the company continue to operate successfully?) to long-term issues (e.g. are we attracting, developing and retaining individuals to be future leaders in 3 to 5 years?).

At the heart of CEO succession planning is the notion that the Board and the CEO work in co-operation to attract, develop and retain high performers who can be tried and tested prior to possibly being offered the CEO role in the future.

### *Selecting a CEO*

The selection of a CEO is the most important task a Board can undertake and it is also probably the most difficult task. Boards should drive the succession process, although normally in collaboration with the incumbent CEO. Boards sometimes select a CEO heir-apparent well in advance of the incumbent CEO's planned departure.

For organisations with good succession planning, the selection of a CEO may appear almost automatic with a suitable successor long identified. However, as executives become more mobile and the typical CEO's job tenure continues to shrink, conventional succession planning may not identify an unequivocally acceptable internal candidate. Many Boards have an obligation to look beyond a company's own executive ranks if they are to find the best available CEO.

The Board must ensure that robust processes are adhered to in the lead-up to the appointment. Experience suggests that the probability of a successful outcome is enhanced if Boards follow a structured appointment process.

Confidentiality is critical throughout the appointment process. Any breach will deter potential candidates and reflect poorly on directors and the company as a whole.



## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### ► 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

### *CEO tenure*

CEOs are increasingly under the spotlight with Boards being prepared to replace them if they consider that their CEO is not performing, or believe that future performance may not be up to the level expected.

A 2011 study on CEO succession<sup>83</sup> found that 14.2 percent of CEOs at the world's top 2,500 companies had been replaced that year. Although this is sharply higher than the previous year's turnover rate of 11.6 percent, it is representative of the historical seven year average of just over 14 percent. The survey also indicated that over the last 12 years, CEOs promoted from within serve longer terms than CEOs hired externally, with an average tenure of 7.6 years (compared to 5.6 years for the 'outsider' CEOs).

Investment in the CEO and management team is crucial for the creation of sustained shareholder wealth. For this reason, directors need to commit considerable time and effort to selecting a new CEO. This should be supplemented by appropriate mentoring, development, encouragement and support; a role often fulfilled by the Chairman of the Board.

When CEO performance concerns arise, these should be discussed and addressed promptly. If it is clear that the CEO is not delivering and needs to be replaced, then the Board should act without delay. Whilst the cost of replacing a CEO is considerable, the cost of not acting can be devastating.

### *CEO appraisal*

The CEO performance appraisal is an important Board responsibility and should take place on an annual basis.

This appraisal provides:

- Important feedback to the CEO about his performance
- Increased understanding of the CEO's concerns and views on the achievement of corporate objectives
- A forum to build a healthy relationship between the Board, especially the Chairman, and the CEO
- A framework for the CEO to further develop capabilities
- A forum to reinforce accountability, transparency and the responsibilities of the CEO
- An opportunity to identify and address early warning signs of possible difficulties
- An opportunity to discuss any future plans the CEO may have (e.g. retirement).

A robust appraisal process should be established that reflects the company's unique circumstances. This work is generally the responsibility of the Remuneration Committee ("RC"), which will make recommendations to the entire Board.

A more accurate picture of CEO performance can be gained by incorporating the views of several groups. For example, directors, institutional shareholders, customers, suppliers and other key stakeholders will all have a view on the CEO's performance. This must be handled sensitively and all comments treated confidentially to uphold the integrity of the appraisal process.

Both quantitative and qualitative indicators may be included to assess the CEO's leadership behaviour and performance goals, which are fundamental to sustained organisational performance. Using financial and company performance measures alone are inherently problematic.

83 Booz and Co., CEO Succession Report 2011 – 12th Annual Global CEO Succession Study

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### ► 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

There are a myriad of factors outside the direct control of the CEO that can affect company performance. A CEO may be performing strongly when the company is not and *vice versa*. Also, shareholder value can be measured from a number of perspectives, with startlingly different end results. In any event, CEO performance should be measured not only against short-term company financial performance, but also on the CEO's own performance, especially against agreed key performance indicators and corporate strategic objectives.

### Executive remuneration

Executive remuneration is a topic that usually elicits much discussion and controversy. There should be a formal and transparent procedure for developing policies on executive and director remuneration<sup>84</sup>. In determining a remuneration policy, the Board needs to:

- Ensure that it is appropriate to attract, retain and motivate the directors to provide good stewardship of the company
- Ensure that remuneration is set at levels that appropriately reward and incentivise management to pursue long-term growth and success
- Demonstrate a clear relationship between senior executives' performance and remuneration
- Ensure that the remuneration policy is understood by investors.

Although levels of executive remuneration have grown worldwide, the key issue of concern to stakeholders is not so much the size of executive pay packets, but rather the potential misalignment with corporate performance.

The right reward mix should be determined by reference to many factors, including the size of the organisation, the industry in which it operates, international presence and market considerations. A well-structured remuneration package will ensure that the CEO (as well as other senior executives) is appropriately compensated with a competitive level of fixed remuneration, together with an at-risk component that is designed to support motivation, encourage retention and has an appropriate focus on the company's short and long-term goals.

The at-risk reward components (which usually comprise a mix of short and long-term incentives) of a CEO's remuneration are becoming increasingly important to executive motivation and retention. Similarly, investors want to see a greater proportion of executive remuneration at risk, with a structure that is more closely aligned with their own interests. In other words, investors want to see executive reward linked to company performance.

In most companies, the greater the accountability an individual assumes, the greater the proportion of variable against fixed remuneration. Public companies globally are reforming executive remuneration policies to achieve a greater alignment between pay and performance. Executive remuneration has been the subject of much debate and increasing focus in recent years.

Changes in director's remuneration packages are required to be approved by a resolution<sup>85</sup>. Listed companies are subject to a strict disclosure regime. Listed companies are required to make specific and comprehensive annual disclosures regarding the company's remuneration framework and the remuneration arrangements for the Board and key management personnel<sup>86</sup>.

84 CG Code Principle 7 and 8

85 CA Section 169

86 SGX LR 1207(15) and CG Code Principle 9

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### ► 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

The Board should establish a formal and transparent procedure for developing policy on executive and director remuneration<sup>87</sup>. The RC is usually tasked to review and recommend to the Board a general framework of remuneration for the Board and key management personnel<sup>88</sup>. The RC may also seek expert advice within or outside the company on remuneration matters. In such cases, disclosures must also be made in the annual report with a statement indicating whether the appointment of the remuneration consultants is free of undue influence by the key management personnel to whom the remuneration recommendation relates<sup>89</sup>.

Companies are encouraged to consider the use of contractual provisions to allow the company to reclaim incentive components of remuneration from executive directors and key management personnel in exceptional circumstances of misstatement of financial results, or of misconduct resulting in financial loss to the company<sup>90</sup> and remuneration arrangements on appointment. It is important that there is sufficient expertise within the ranks of the RC to effectively advise the Board on these matters. The Board is ultimately responsible for ratifying the appointment of the CEO, and thus it should retain sign-off authority.

It is important that the process adopted ensures that the executives for whom contracts are being negotiated remain at arm's length (i.e. instructions on the preparation of the contract should be given directly to solicitors or consultants by the RC). This does not preclude the CEO and other senior executives from making submissions to the RC about their own contracts or making recommendations on the remuneration of their direct reports.

87 CG Code Principle 7  
88 CG Code Guideline 7.2  
89 CG Code Guideline 7.3  
90 CG Code Guideline 8.4

The preparation of an executive service agreement is complex. Professional advisers should be engaged who can ensure that the contract reflects what has been agreed and that the contract accords with the law. Any drafting of contracts needs to consider the regulatory framework and the company's governing documents, including the:

- CA
- SGX LR
- Industrial relations, employment and WH&S legislation
- Company Constitution
- Company remuneration policies
- Company strategy

### Executive service agreements

With more rigorous disclosure requirements, the Board's approach to negotiating the terms of CEO and senior executive service contracts is more open to challenge by the media and shareholders.

The Board has the difficult task of striking a balance between the need to attract and retain senior executives with protecting company interests by not paying 'excessive' remuneration. Most importantly, the process by which executive service agreements are set up must be transparent and beyond reproach.

The RC is usually vested with the responsibility of providing recommendations to the Board in relation to the key terms of executive service agreements and remuneration arrangements on appointment. It is important that there is sufficient expertise within the ranks of the RC to effectively advise the Board on these matters. The Board is ultimately responsible for ratifying the appointment of the CEO, and thus it should retain sign-off authority.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
- 04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

# 4. Productive Meetings

The way the directors' meetings are run says much about how a company is being managed. Directors' meetings should be carefully scheduled, prepared to facilitate forums for informed discussions and decisions and to improve key business strategies.

## Questions that company Directors should ask

- |  |  |
|--|--|
| 1. Is the number and length of Board meetings sufficient to allow the Board to effectively discharge its duties and responsibilities?            | 6. Is the size of the meeting group appropriate, having regard to the purpose of the meeting, and are all attendees directly relevant? |
| 2. Are Board members able to access the previous meeting's Board minutes with ease and review these prior to the next Board meeting?             | 7. Is regular feedback and evaluation of the effectiveness of meetings provided to Board members?                                      |
| 3. Are all Board members provided sufficient time to review the Board papers prior to entering the meeting?                                      | 8. Does the Board manage actions arising from Board minutes, with outstanding actions being reviewed at each Board meeting?            |
| 4. Is the Chairman clearly accountable for the agenda's content, with all directors and committee Chairmen having the opportunity to contribute? | 9. Is the Board undertaking critical self-assessment to identify opportunities for improvement?  |
| 5. Are communication channels used by the Board to conduct its business secure and confidential?   |  |

## Red flags

- |  |   |
|--|---|
| ► Board or sub-committee meetings are not scheduled on a regular basis   | ► Attendee and absentee lists are kept irregularly and sometimes not noted in the minutes   |
| ► Meeting agendas and materials are not circulated in advance, hence not allowing for adequate time for review | ► There is no information sharing portal set up for the Board and directors rely on emails and hand-outs to communicate and store information |
| ► The Company Secretary provides incomplete or late distribution of Board meeting minutes after meetings       | ► Meetings are usually closed without an agreed set of actions  |
| ► Many issues discussed are carried over to the next meeting   | ► The modes to exchange and store information and documents are not secured   |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
- 04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Duties related to Board and committee meetings

As organisations are getting more complex, directors are expected to be fully prepared for Board meetings. Board papers should be read in advance as directors are expected to contribute meaningfully to Board meetings in order to discharge their director duties. A director's meeting attendance record is often taken into account by the NC in consideration for re-election to the Board.

Unless the company's Constitution provides otherwise, the quorum for a directors' meeting is two directors, and the quorum must be present at all times during the meeting<sup>91</sup>.

Each director needs to be aware of the requirements relating to the conduct of Board meetings as set out in formal documents such as the Board charter and the company's Constitution.

### Roles and responsibilities to host productive meetings

The Chairman has the most influence in any Board meeting and plays a pivotal role in the effective functioning of meetings, maintaining responsibility for leadership of the Board and its efficient organisation and functioning<sup>92</sup>. The Chairman's key role is to lead discussions, encourage participation of and interaction amongst members, prevent any one director dominating the discussion, conduct meetings in an effective manner i.e. summarise what has been decided to avoid misunderstandings, be firm in allocating responsibilities and making sure that they are carried out and that all decisions have been put into practice, promote high standards of corporate governance

and ensure that there is sufficient time devoted to discuss pertinent matters.

The Chairman should receive regular feedback on what could be improved. Some companies have used a non-executive to carry out a regular appraisal by gathering feedback from the whole Board<sup>93</sup>.

The Company Secretary is also instrumental in ensuring that meetings are conducted smoothly by being proactive and anticipatory of directors' needs and should ensure:

- Board agenda and briefing materials are completed and circulated timely
- Invitations have been sent to the appropriate personnel to the meeting
- Presentations are concise and highlight significant issues
- Chairman is appropriately briefed and supported
- Meeting venue and location is appropriate and secure
- Audio-visual and other equipment is operational
- Expert or professional advice is available when required
- Meetings begin and end promptly at the scheduled times
- Be aware of particular customs, rules and etiquette for the meeting.

Board committees provide an effective way of distributing work between directors and allow for more detailed consideration of important issues. There is also greater opportunity to focus on relevant matters without having to compromise the limited time available during full Board meetings.

91 CA Section 179(1)(a)

92 CG Code Guideline 3.2

93 ICAEW, *Effective Board meetings*, [www.icaew.com/~media/Files/Library/collections/online-resources/briefings/directors-briefings/ST5EFFEC.pdf](http://www.icaew.com/~media/Files/Library/collections/online-resources/briefings/directors-briefings/ST5EFFEC.pdf)



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
- 04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Agenda

It is useful to set and cascade the Board agenda in advance to all directors as this enables directors to be fully informed of items to be proposed and discussed at the meeting. This agenda should be referenced to the annual agenda.

The Chairman and Company Secretary should take responsibility for the content of the agenda, seeking input from other attendees such as other committee members, the CEO and senior management. After which, the Chairman decides on the final content of the agenda. The agenda should provide an overview of the content, the ordering of items, the allocation of time for each item and deciding on invitees. Time should be allocated to items according to their importance and it is also essential to categorise items which are for decision, discussion, noting or information purposes. A timed agenda will assist directors in recognising the relative significance of each issue and ensure the meeting ends on time.

The agenda below shows a typical structure:

1. Approval of the minutes of the last meeting  
Board members can highlight errors or to add points which have been left out.
2. Matters arising  
Members are invited to raise issues which are not due to be covered in the published agenda.
3. Strategic issues  
For example: Discussion on the acquisition of another company or the creation of a new company department.
4. CEO's report  
This may cover major new initiatives, the business outlook, foreseeable threats and opportunities, review of ongoing projects and operational issues.

5. Presentation of financial reports  
This is a review of the company's financial performance.
6. Procedural and compliance issues  
For example, this may include the appointment of a new director.
7. Any other business
8. Date of next meeting

### Meeting preparation

Careful preparation of the agenda enhances the Board's productivity and supports its strategic and oversight role. The Board meeting should be an opportunity for directors to add value to the discussion and decision instead of being informed of the issues for the first time. There should not be any surprises. In fact, one of the Chairman's duties is to apprise members of any sensitive issues in advance.

When the agenda and purpose of the meeting is communicated to members in advance, this allows them to become familiar with the proposed agenda and raise questions or undertake research prior to the Board meeting. The purpose of the meeting should be linked to a specific plan or outcome.

### Meeting attendance

Attendance at meetings is part of discharging the duties of a director. Directors should be present for Board and appropriate committee meetings. Absenteeism will never excuse a director from their duties to the company. To facilitate participation, directors may attend in person, via teleconference or video-conference.

Directors who are unable to attend a meeting should notify the Board in advance and the absence with apology should be documented in the minutes of meeting.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
- 04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

The number of meetings of the Board and Board committees held in the year, as well as the attendance of every Board member at these meetings should be disclosed in the company's annual report<sup>94</sup>.

If there are repeated absences on the part of a director, the Chairman should meet with the director to assess their future availability and commitment. The Chairman may have to decide whether it may be in the company's interest for the director to resign or continue serving on the Board.

### *Meeting frequency and duration*

Both the frequency and duration of meetings are factors which influence the quality of Board discussions. There are no regulations in Singapore that prescribe the number of directors' meetings that must be convened. However, to have an effectively functioning Board, an annual agenda should be set in advance every year. In Singapore, the Board typically meets at least twice a year (for companies which are required to report half yearly results) and for those which have to report quarterly results would meet at least 4 times in a year. There could be ad hoc meetings organised as and when there are important matters to be deliberated.

When planning the agenda for a long meeting, it may be useful to consider whether splitting the meeting into shorter meetings or to hold the meeting offsite, for example a Board retreat day. Scheduling breaks in between the meeting is important to keep participants focused, attentive and productive. The length of the meeting should also allow sufficient time and attention given to all issues.

### **Access to meeting papers and technology**

Board papers should be concise documents that fully present the information the Board will require to comprehend all issues and make appropriately informed decisions. They should be prepared to strict standards in terms of presentation and content, share a consistent format and include the date, version reference, author's name and title.

Technology is rapidly moving into boardrooms, with the digital distribution of Board papers becoming increasingly widespread. Whilst electronic communication methods may facilitate the exchange of timely and accurate information between Board members, companies must also consider the adequacy of the security of confidential data sharing and storage technology such as email, iPad and dropbox-type applications. The use of online portals for hosting Board papers and other company materials is growing substantially as a secure, efficient and economical way of facilitating Board meeting process.

Additionally, a directors' meeting can be called or held using any technology, provided the Board has all directors' consent. Emergency meetings called at short notice may not allow all directors to physically meet and the use of technology such as teleconferences or video conferences enables issues needing prompt attention to be discussed. Face-to-face meetings are often preferred especially where contentious matters are to be discussed.

It is fundamental that where technology is used, that it is secure, reliable and fully functional especially given the commercially sensitive and nature of discussions.

94 CG Code Guideline 1.4

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
- 04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Confidentiality

Consistent with their fiduciary duties, directors are expected to maintain the confidentiality of the matters discussed. Confidential company papers must remain secure. It is leading practice for directors to return meeting papers to the Company Secretary after the meeting, who will then arrange for the secure destruction of those documents.

Several fundamental security recommendations include:

- Encrypting documents
- Installing password-protection mechanisms for all electronic equipment
- Activating automatic locking after periods of inactivity on electronic devices
- Careful use of PINs for conference calls.

### Boardroom conduct

While each Board will have its own particular boardroom style, there are several principles of good boardroom practice and etiquette:

- Be punctual and attend the full meeting
- Be attentive; listen and contribute to the discussion
- Adhere to the timing and agenda of the meeting.

### Meeting procedures

A meeting should only be held if it is necessary. If the same information could be covered in an email or report, for example where all agenda items are information sharing, a meeting should be avoided. As meetings are costly, the outcome must be valuable enough to justify holding the meeting.

It is crucial that Board members have sufficient notice of forthcoming meetings. Circulation of a list of prearranged

dates is sufficient notice and typically a convenient practice.

### Decision-making process

The emphasis in the boardroom is on consensus decision-making, which focuses on securing the agreement of the full Board. If unable to reach a consensus, the Board should state the reasons for this and make effort to solve the issues or find further information required to make a decision.

The Board and management should agree on having a number of predetermined elements included in all material proposals for Board decision. However, these elements should only be used as guidance, and that management exercises common-sense and business acumen in deciding what information to provide to the Board.

The following elements at a minimum should be considered in material proposals for informed decision-making:

- Alignment with strategic direction
- Financial impact and considerations
- Economic and financial assumptions
- Key risks and dependencies
- Legal and regulatory obligations
- Availability of resources (internal and/or external)
- Ethical and environmental dimensions
- Shareholder and stakeholder perspectives
- Description of due diligence completed
- Benefits or outcomes that are measurable and can later be tested
- Contingencies to deal with unexpected developments
- Monitoring and accountability mechanisms.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
- 04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Decision-making outside the boardroom

There will be situations where decisions need to be taken before the next scheduled directors' meeting. It is usually permissible to circulate a resolution for approval by directors without the need to convene a meeting, though this process should be reserved for urgent matters or more procedural matters. The resolution must be signed by all directors entitled to vote on the matter and it is deemed as being passed when all directors have signed<sup>95</sup>. Once the resolution has been passed, it must be minuted and noted at the next meeting of directors.

### Meetings without management

It is also productive for the Board to meet without the presence of management. These meetings usually involve discussion of topics on:

- CEO performance and remuneration
- Relationships between directors
- Strategic matters
- Relationships with management and assurance providers
- Director performance issues
- 'Tone at the top' concerns
- Whistleblower issues relating to senior management
- Confidentiality issues and potential conflicts of interest
- Independence concerns relating to assurance providers
- Sensitive matters affecting management and/or assurance providers
- Internal / external audit.

Formal action plans pertaining to the above discussions should be documented and tracked in subsequent meetings.

### Board minutes

The company is required to document and keep a record of the minutes of general meetings and other meetings within one month of the meeting held<sup>96</sup>. The company is required to retain records up to a period of 5 years<sup>97</sup>. The minutes must also be signed within a reasonable timeframe. The minutes shall be open for members to peruse without charge<sup>98</sup>. Minutes should be documented very carefully, and with due regard to being potentially referred to as documents with legal significance in instances of litigation. It is therefore paramount that directors review and approve the minutes carefully and give them the level of attention they warrant, rather than simply treating their approval as an administrative exercise. Once signed, minutes are evidence of a proceeding, resolution or declaration to which it relates. Criminal penalties can be imposed for the falsification of records. If inadvertent errors are detected in signed minutes, directors may pass a resolution at a future meeting to correct them. The directors may agree not to proceed with an agreed course of action as set out in the signed minutes. In these circumstances, it will be necessary for the directors to pass a resolution to rescind previous resolutions.

The minutes should be formally approved at the next Board meeting and if the minutes are amended, this should be reflected in the minutes of the subsequent meeting.

95 CA Section 188(3B)

96 CA Section 188

97 CA Section 199(2)

98 CA Section 189 (1)

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### ► 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

The company is required to keep the Board minutes books at the company's registered office or its principal place of business in Singapore<sup>99</sup>.

The level of detail included in the minutes will vary from company to company. General inclusions would be:

- Company name
- Meeting venue, date and commencement time
- Chairman and attendee names, including those physically present and those participating through the use of technology (e.g. teleconference)
- Absence with apologies
- Presence of a quorum
- Minutes of the previous meeting
- Directors' declarations of personal interest
- Proceedings and resolutions (including a brief outline of material factors in reaching a decision)
- Title, version reference and date of all papers tabled
- Action plans, timelines and responsibilities for implementation
- Closure time
- Signature of the Chairman (at the subsequent meeting).

## Meeting evaluation

The meeting should conclude with decisions agreed. All directors should be aware of the action plans that require their attention for discussion in subsequent meetings. Following a meeting, the Company Secretary should distribute minutes promptly to allow directors to respond timely and for issues to be discussed more meaningfully in the next Board meeting.

## Board self assessment

A useful tool for obtaining feedback to further enhance the Board's meeting productivity is to obtain an independent assessment. This can be gathered through conducting surveys, completing questionnaires and observation of the Board members and meetings, combined with benchmarking to high performing Boards. This process will assist the Board in identifying its strengths and potential opportunities for improvement. The process also provides assurance to shareholders and employees that the Board is proactively seeking feedback to drive continuous improvement.

99 CA Section 189(1)



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
- 05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

# 5. Ethical Culture

Developing an organisational culture of ethics and compliance is a business imperative. Culture is the basic fabric of an organisation that shapes 'how we do business here'<sup>102</sup>.

## Questions that company Directors should ask

- |  |   |
|--|---|
| 1. Are the code of ethics and conduct and compliance program regularly reviewed to determine if they need updating due to business, legal or regulatory changes?                           | 6. Has a corporate culture been developed and maintained that creates an environment of openness, honesty and the immediate reporting of bad news?                    |
| 2. Has the organisation's ethics and compliance program been reviewed by outside consultants or experts for possible improvement?  | 7. Does management fully inform the Board about potential or actual conflicts between the company's values and the business practices in countries where it operates? |
| 3. Have any compliance investigations arisen from a cultural problem?  | 8. Are there processes and practices in place to promote ethical behaviour?   |
| 4. Is there an effective whistleblowing process in place?  | 9. Has the Board considered how executive compensation aligns with the desired ethics and compliance culture?   |
| 5. Do individuals receive the information required to understand the firm's core values, code of ethics and conduct and the specific policies, laws and regulations related to their jobs? |   |

## Red flags

- |   |   |
|---|---|
| ► The Board has power factions that inhibit teamwork                | ► The Board receives no reports or information regarding the whistle-blower policy                              |
| ► The Board suffers from a 'group think' mentality                  | ► The Board virtually 'ticks the box' for CEO recommendations   |
| ► The code of conduct has not been reviewed in recent years         | ► The Board culture does not allow discussion of difficult, controversial or sensitive matters in the boardroom |
| ► There are a concerning number of internal and external complaints |   |

<sup>102</sup> KPMG, Survival of the Most Informed: GRC Comes of Age – How to Envision, Strategize, and Lead to Achieve Enterprise Resilience, 2010.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
- 05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### 'Tone at the top'

Ethics and compliance programs are often initiated in response to legal requirements and other guidelines, though it is important that the program is more than just adherence to rules and policies. Instead, it should embed an ethical culture into an organisation<sup>100</sup>. Merely meeting legal requirements is unlikely to be sufficient to satisfy the ethical concerns of employees, clients, customers, shareholders and other stakeholders.

The commitment of the entire organisation is essential in order to design, develop and implement an effective ethics and compliance program. Boards set the 'tone at the top', which influences the entire organisation. The Board should ensure that appropriate values, ethics and culture are upheld throughout the organisation.

The 'tone at the top' refers to the character and behaviour displayed by leaders of an organisation that forms a model of appropriate conduct for every level of the organisation. Boards bear ultimate responsibility for their organisation's culture, including the values and ethical environment that underpin that culture.

The 'tone at the top' should be underpinned by clearly articulated values and policies, a code of ethics and conduct, ongoing ethical awareness training and an ethics management process that is embedded across all the organisation's activities.

### Business ethics

The Board is responsible for setting the company's values and standards (including ethical standards)<sup>101</sup>.

Business ethics refers to rules, standards, stated organisational values and behaviours that determine what is acceptable or unacceptable in specific situations. They are inextricably linked to notions of honesty, integrity, trust, accountability, transparency and social responsibility<sup>102</sup>. Ethical conduct is a key factor in the long-term viability and success of organisations. Moreover, the reputations of individual directors and executives are tarnished when a business is seen not to have acted ethically, or has otherwise breached community standards.

An organisation's business ethics and corporate culture may be revisited in conjunction with a Board review or a review of the organisation's pay practices. Perceived failures, adverse media exposure and episodes of high staff turnover are examples of possible catalysts for a re-awakening interest in business ethics and corporate culture; a tool to revitalise the organisation.

An effective business ethics process should generate real benefits, including:

- Increasing the integrity of financial reports and information
- Minimising the incidence and encouraging the reporting of fraud and other organisational misconduct
- Creating confidence that unethical behaviour will be reported and addressed
- Producing a working environment that fosters pride, responsibility and a sense of both purpose and value.

<sup>100</sup> KPMG, The Road to a Model Ethics and Compliance Program, 2009.

<sup>101</sup> CG Code Guideline 1.1(e)

<sup>102</sup> KPMG, A view from the top – Business Ethics and Leadership, 2005.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
- 05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

The following is an example of a business ethics framework:

- A code of ethics that clearly and concisely articulates an organisation's values and behaviours
- A code of conduct which underpins all organisational activities, sets out the organisation's employment practices, and that provides direction on how management will manage the business. Ethics and awareness training should be delivered and reinforced regularly to all employees, and included in induction programs for new employees
- Formal processes providing guidance to employees facing ethical dilemmas, and the mechanisms for reporting wrongdoing and making suggestions about how business ethics can be improved
- A performance management process that not just measures results, but considers how these results have been achieved.

### Organisational values and ethics

Organisational values not only guide a company's people, but also create expectations on the part of external stakeholders about acceptable behaviour within the organisation. Strong values shared by both an organisation and its employees have been found to increase employee commitment and satisfaction.

Once agreed, values should be embedded in documented policies and procedures, and then actively embraced and practised by all company personnel. An effective ethics and compliance program requires senior management involvement to entrench and uphold values, organisation-wide commitment, an effective communications system and an ongoing monitoring system.

### Code of ethics and conduct

Good corporate governance is ultimately about personal and organisational integrity. Though this cannot be regulated, investor confidence can be enhanced if the company clearly articulates acceptable practices for directors, senior executives and employees.

Typically, a code of ethics:

- Spells out an organisation's values and principles
- Reflects and shapes the organisation's culture
- Makes transparent the value framework within which the organisation operates.

The code of ethics is complemented by the code of conduct. The Directors' Code of Professional Conduct ("Code of Conduct") incorporates the values adopted by SID, and has been published to ensure that all directors are committed to achieving the highest level of professionalism and integrity in the discharge of their office. The Code of Conduct is intended to complement the CG Code.

The Code of Conduct embraces the values of honesty, integrity, personal excellence and accountability which should be the cornerstone of every director's conduct. While the Code 2012 sets out principles of corporate governance to be observed by listed companies, the Directors' Code of Conduct amplifies the standards of ethics which should be adopted by individual directors in order to bring about the highest standards of conduct in the discharge of their duties.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
- 05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

The Code of Conduct adopted by SID addresses the following attributes that a director should possess:

- The practices necessary to maintain confidence in the company's integrity
- The practices necessary to take into account the company's legal obligations and the reasonable expectations of stakeholders
- The responsibility and accountability of individuals for reporting and investigating reports of unethical practices
- Personal standards and values in being honest and avoiding perceived or actual conflicts of interest.

As the Board and senior executives are responsible for setting the tone and ethical standards of the organisation and overseeing adherence to them, they must demonstrate that the agreed codes and standards are equally applicable to them and lead by example.

Organisations that 'walk the talk' with regard to their code develop a reputation for honesty, integrity and principled business behaviour, which may form a key element of a company's brand and enhance its reputation<sup>103</sup>.

When overseeing the implementation of the code, directors must ensure that it is effectively communicated by management. The Board should make certain that the code of ethics and conduct is taken seriously throughout the organisation, and that breaches will give rise to disciplinary measures.

Merely issuing a code, however, does not ensure that it will be observed. To add value, the code must extend beyond a compliance focus and strive to cultivate and maintain an organisation-wide culture that focuses

on encouraging positive moral behaviour while simultaneously striving to prevent ethical lapses<sup>104</sup>.

The code must continue to evolve with the changing environment. This includes laws and regulations, the operational environment, public opinion and focus on acceptable business behaviour. Those developing or

revising the code of ethics and conduct should consult frequently with legal experts and other specialists in areas addressed by the code.

## Cultural issues

### Global operations

Companies with significant global operations face additional difficulties in evolving and implementing codes of ethics and conduct. In part, it is a matter of different cultural norms — what is generally acceptable in Singapore might not be so acceptable in another country.

The Board should be fully informed about conflicts between the company's values and business practices in various countries as a lack of understanding of cultural differences may contribute to a lack of performance, loss of key employees and time consuming conflicts.

Multinational companies are faced with several issues:

- How to foster a culture of ethical conduct in all countries of operation
- How to engage a global workforce in understanding and adopting its corporate values
- How to meet all the legal and compliance obligations throughout all locations
- Language barriers between different global units.

<sup>103</sup> 20 Questions Directors Should Ask about Codes of Conduct, Gunns. M & Wexler, M. 2010

<sup>104</sup> K. M. Gilley, C. Robertson, T.C. Mazur, The bottom-line benefits of ethics code commitment, 2010.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
- 05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

When selecting leadership roles within a multinational company, cultural 'fit' may be a relevant consideration, in an attempt to promote consensus on a global, organisation-wide culture, particularly when appointing local leaders across international business units.

A failure to consider an organisation-wide code of conduct may lead to significant cultural differences in the executive levels of the company around the world, potentially fostering a lack of understanding and commonality of purpose that may lead to conflict and poorly communicated decisions. Global principles, based on corporate values, should be promoted across the organisation, while still allowing for local cultural traditions within international business units.

### Mergers and acquisitions

A 2016 KPMG survey<sup>105</sup> revealed that cultural and human resource issues are major post-deal issues and companies frequently associate integration issues with cultural variation and complexity. While such issues are pre-empted, organisations tend to place higher importance on areas such as strategic fit, growth potential, and the target's valuation and investment return. The issue of cultural compatibility is of the least concern to companies.

Central considerations in managing the integration of company cultures include:

- Closeness of cultural fit
- Implications for future ways of working
- Retention of, and rewards for, key people
- Understanding what makes the business successful, and how this will be retained and built on.

It should be considered whether the cultures of the two organisations are compatible, and if one will be dominant, how employees operating under the alternative culture will be embraced. If one culture is to prevail, retaining key leaders of that organisation to serve as role models is essential in order to promote the integrated culture. A key objective in a merger or acquisition is to incorporate the advantages of each organisation's culture, ultimately resulting in synergy. A plan for the merging of cultures should be devised, incorporating educational efforts to assist employees to understand the corporate values they should adopt in the workplace.

Difficulties encountered in mergers and acquisitions are amplified in cross-cultural situations involving multinational companies.

### Developing a culture where 'bad news' is communicated

Recent corporate scandals highlight the importance of building a corporate culture that supports the giving and receiving of 'bad news' i.e. creating an environment of openness and honesty and the presentation of the hard truth.

A KPMG-sponsored survey found that only 55 percent of respondents believe that their organisation is effective at keeping the Board aware of the key risk issues.<sup>106</sup>

A culture where an early warning system for problems exists can provide for timely and appropriate intervention and/or the redefining of strategy. A climate in which full disclosure is delivered in a timely manner should be fostered by senior management and endorsed by the Board to encourage employees to immediately bring forth concerns.

<sup>105</sup> KPMG, U.S., executives on M&A: full speed ahead in 2016

<sup>106</sup> A report from The Economist Intelligence Unit sponsored by ACE and KPMG (The Economist) (2010)



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
- 05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Whistleblower policy

The term 'whistleblower' refers to anyone who alerts superiors or the appropriate authorities to misconduct within an organisation. All employees and any other persons should be encouraged to raise genuine concerns about possible improprieties in the conduct of an organisation's business<sup>107</sup>.

Employees may fear retaliation if they take their concerns to management or believe their allegations will not be taken seriously. They might not know who they should take the matter up with, and this becomes a more acute concern when the subject of the allegation is their manager or someone more senior.

Whistleblowing measures will yield little unless employees trust the system and are comfortable using it. It is possible that if employees believe their complaints will be ignored or covered up, or that complainants will be victimised, they may take their concerns directly to the news media or law enforcement agencies. Effective codes provide whistleblowers with several channels to speak candidly and confidentially about ethical concerns in order to improve the likelihood that individuals will first seek to resolve issues and concerns internally<sup>108</sup>.

Many companies use externally operated anonymous, independent fraud and misconduct reporting services to eliminate the fear of retaliation. These services usually provide staff with a toll-free telephone number for reporting their concerns about fraudulent or improper conduct. All whistleblower reports should be investigated and reported to the Audit Committee. Some companies appoint an investigations officer for this purpose.

The Audit Committee should review the policy and arrangements by which staff of the company and any other persons may, in confidence, raise concerns about possible improprieties in matters of financial reporting or other matters. This is to ensure that arrangements are in place for such concerns to be raised and independently investigated, and for appropriate follow-up action to be taken. The existence of a whistleblowing policy should be disclosed in the company's annual report, and procedures for raising such concerns should be publicly disclosed as appropriate<sup>109</sup>.

At present, there are several statutory provisions that offer some form of protection for whistleblowers. Section 36 of the Prevention of Corruption Act ensures that a complainant's identity will not be disclosed, even during court proceedings, unless the court finds that he has wilfully made a false statement in their complaint. Similarly, Section 208 of the Act offers protection to company auditors by ensuring that they will not be liable for defamation for any statement made in the course of their duties.

### Boardroom dynamics

Board culture underpins Board dynamics and has a decisive influence on performance. A well-functioning Board generally displays coherence, trust and common values between members, encourages and has regard to differing viewpoints and opinions, and is able to reach a decision without animosity. Healthy boardroom dynamics will encourage sound decision-making that delivers value to shareholders.

<sup>107</sup> CG Code Guideline 12.7

<sup>108</sup> 20 Questions Directors Should Ask about Codes of Conduct, Gunns. M & Wexler, M. 2010

<sup>109</sup> CG Code Guideline 12.7

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
- 05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

The working relationship between directors and management is one of the most influential factors in Board effectiveness. Most productive relationships are built on mutual trust and respect, where both the Board (and the Chairman in particular) and the CEO work in partnership, each with an acute appreciation of the vital role played by each other in building shareholder value. Dysfunction can occur where either the Chairman or the CEO is overly controlling and this behaviour goes unchecked.

### Informal communications outside Board meetings

Informal communication is one of the most effective ways of sharing information, building knowledge and fostering constructive working relationships. For this reason, Boards that communicate regularly, when necessary, with each other and management, are typically strong decision-makers.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
- 06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

# 6. Board's Governance Roles and Conduct of Affairs

There are many instruments, roles and responsibilities required for a Board to deliver its governance function effectively. Key factors such as independence, Board composition and skills are vital in delivering strong Board performance.

## Questions that company Directors should ask

- |  |  |
|--|--|
| 1. Is the composition of the Board appropriately diverse for it to perform effectively?  | 5. Does the Board tailor its charter to the company's evolving operating environment and is the charter periodically reviewed? |
| 2. Is the Board sufficiently independent of management to enable it to make challenging decisions?                                       | 6. Does the Board periodically review the Board's and Chairman's performance?  |
| 3. Is there a regular assessment of each director's independence made by the Board and is the process effective?                         | 7. Are matters that must be referred to the Board for approval clearly communicated to management?                             |
| 4. Is there an annual agenda, approved by the Board that is linked to the Board's key responsibilities as detailed in the Board charter? | 8. Are delegations to management, including the delegations policy documented?   |

## Red flags

- |   |  |
|---|--|
| ► The Board is heavily weighted towards a certain skill set, background, or gender                      | ► A statement of 'matters reserved for the Board' has not been prepared, nor is it publically available  |
| ► Some directors have family ties or cross-directorships that have not been discussed or are overlooked | ► Matters reserved for the Board' implies limits on the CEO, but is not explicit and clear, resulting in various assumptions and interpretations |
| ► Assessments of director independence are informal and infrequent                                      | ► Directors sit on too many Boards and not being able to dedicate time to the company  |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
- 06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

The Board is responsible to lead the company to achieve its objectives.

The Board's governance scope should include the following key functions<sup>110</sup>:

- Provide entrepreneurial leadership, set strategic objectives, and ensure that the necessary financial and human resources are in place for the company to meet its objectives
- Establish a framework of prudent and effective controls which enables risks to be assessed and managed, including safeguarding of shareholders' interests and the company's assets
- Review management performance
- Identify the key stakeholder groups and recognise that their perceptions affect the company's reputation
- Set the company's values and standards (including ethical standards), and ensure that obligations to shareholders and other stakeholders are understood and met
- Consider sustainability issues, e.g. environmental and social factors, as part of its strategic formulation.

### Board Charter

The purpose of a Board charter is to document the Board's terms of reference and to articulate the Board's approach to important governance practices. The charter should contain a statement clarifying the division of responsibilities between the Board and management. Many Boards define the roles, powers and the responsibilities that it specifically reserves for itself, and those which it delegates to management.

While the content of the Board charter will vary from company to company, the Board charter of a listed company will typically cover matters such as:

- Board's roles, functions and responsibilities
- Board's structure/ committees, composition and independence
- Chairman's and CEO responsibilities
- Board meeting procedures
- Assessment and evaluation of Board's performance
- Policy in developing the directors' remuneration policies
- Assessment over company's performance and prospects
- Oversight of strategy, financial, risk management and internal controls
- Shareholders' engagement
- Reporting and records.

The Board charter should be periodically reviewed by the Board to ensure that the charter remains relevant to the circumstances of the company. The charter should also be available to directors, management and staff, auditors and shareholders. See [Appendix 1](#) for an example of a Board charter.

### Annual Board agenda

Boards commonly formulate an annual Board agenda as an effective planning tool. The Chairman should refer to the annual agenda before approving the agendas for individual Board meetings.

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### ► 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

An effective annual agenda will:

- Provide coverage of all the Board's key activities
- Provide adequate time for discussion
- Ensure all the obligations included in the charter will be addressed
- Provide opportunities for the continuous development of directors
- Consider current and emerging issues relevant to the directors' role, company and industry
- Provide an opportunity for self-assessment of the Board's performance agenda.

See [Appendix 2](#) for an example of a Board annual agenda.

### Retained Authorities

A company should prepare a document with guidelines setting forth matters reserved for the Board's decision and clear directions to management on matters that must be approved by the Board. Material transactions requiring Board's approval should be disclosed in the company's annual report<sup>111</sup>.

Some of these responsibilities may include:

- Responsibility for the overall strategic oversight of the company
- Review changes to company's capital structure
- Approval of financial policies and announcements
- Ensuring maintenance of a sound system of internal control and risk management
- Monitoring and approving major investments and contracts

- Reviewing matters pertaining to shareholders communications
- Reviewing Board membership and senior executive appointments
- Assessing remuneration of Board members and management
- Ensuring an adequate and effective Delegation of Authority framework is in place to provide clear direction to management and the Board
- Reviewing independence of directors.

The relative importance of some matters included in the above may vary according to the size and nature of the company's business.

### Delegated authorities

Given the complexity and size of the typical large organisation, it is not possible at all times for a Board to exercise all of its functions and powers. A director may delegate some duties to other directors or key executives of the company.

The Constitution of a company typically outlines the mechanisms for directors to delegate powers to committees. However, the director cannot delegate all responsibilities to another person to absolve him from exercising proper supervision and managerial control over the company. S157(C) of the Act accords protection to directors for reasonable reliance on information and advice prepared or provided by employees, professionals and experts with respect to matters within their own areas of competence; however only if the director has acted in good faith and made proper inquiries.

111 CG Code Guideline 1.5



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
- 06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

The Board may also delegate authority to make decisions to any Board committee without relinquishing its responsibility<sup>112</sup>. Such delegation should be disclosed<sup>113</sup>. A common example and as contained in The Guidebook for Audit Committees in Singapore (Second Edition) [Guidebook for ACs], provides guidance on the Board delegating duties to the AC to the extent that the AC has the time and skills to discharge them. In addition, the Board should also have a procedure for directors to take independent professional advice at the company's expense. It is important that directors do not review materials and financial reports presented by management and auditors on face value. Questions should be asked where necessary so as to obtain comfort that the work of management and external consultants can be relied on.

The delegations policy, which is approved by the Board, should specify the limits of authority for all individuals. This will assist the Board to fulfil its duty of care and a useful reference to all company personnel as to who has responsibility for decision making for the various types of business transactions and matters.

<sup>112</sup> CG Code Guideline 1.3

<sup>113</sup> CG Code Guideline 1.3



## Case Study

In the case of Rio Tinto, Tom Albanese, who was the CEO at that time had to step down from his role in 2013 after AUS\$13 billion worth of write-downs on the company's aluminium assets and its coal division in Mozambique. The projects were two of Mr. Albanese's most significant acquisitions. Brendon Booth of Human Capital commented that "the CEO has ultimate responsibility", but "has to delegate and push down the responsibility, so other people are making critical decisions."



The matter of delegated authorities is faced by companies globally as directors and executives often need to make decisions, be it with regards to acquisitions or day-to-day operations of the organisation. This particular case highlights the need for a robust Board-approved delegations policy, which specifies the limits of authority for all individuals.<sup>1</sup>

<sup>1</sup> <http://www.abc.net.au/news/2013-01-17/rio-tinto-ceo-to-stepdown/4470040>, "Rio Tinto chief quits after heavy write-downs" and <http://www.smartcompany.com.au/leadership/29918-why-rio-tinto-gaveits-ceo--tom-albanese--a-push.html>

## Foreword

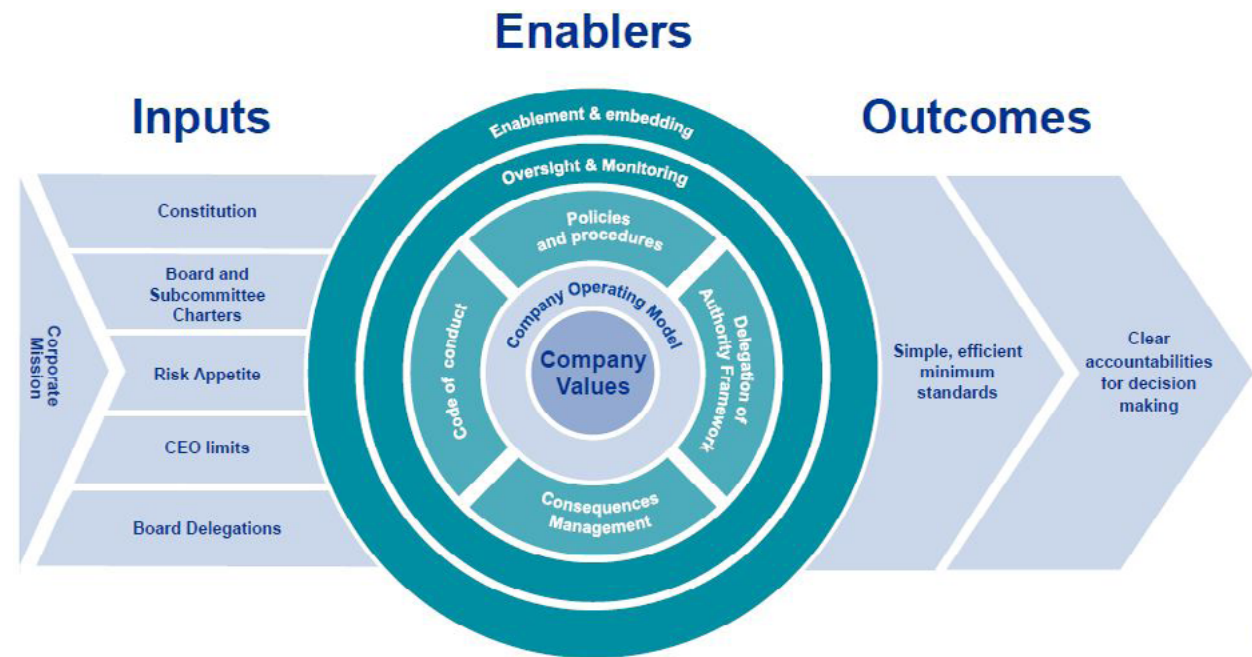
01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
- 06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Accountabilities framework

It is the Board's responsibility to provide a balanced and understandable assessment of the company's performance, position and prospects and these extend to providing interim and other price sensitive public reports,

and reports to regulators<sup>114</sup>. As such, adequate steps should be taken to ensure compliance with legislative and regulatory requirements under the listing rules of the securities exchange<sup>115</sup>.

### KPMG accountabilities framework



The KPMG accountabilities framework above is designed to deliver simple, efficient standards and clear accountabilities for decision-making across the organisation. To achieve an effective accountabilities framework, it requires the Board to endorse these instruments, oversee their implementation and regularly consider their compliance.

### Non-executive directors

There are two principal types of directors: executive directors and non-executive directors. A non-executive director is someone who is not employed by the company and not engaged in the day-to-day management of the company.

<sup>114</sup> CG Code Principle 10 & Guideline 10.1

<sup>115</sup> CG Code Guideline 10.2

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
- 06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

Commonly, non-executive directors have key responsibilities to deliver including<sup>116</sup>:

- Constructively challenge and help develop proposals on strategy i.e. having the characteristics and strong ability to confront management and receive satisfactory responses to any difficult questions that are raised
- Review the performance of management in meeting agreed goals and objectives and monitor the reporting of performance.

Non-executive directors are encouraged to meet regularly without the presence of management to have a more effective check on the latter<sup>117</sup>.

Additionally and according to the Higgs report<sup>118</sup>, effective non-executive directors should possess key personal attributes, in order to discharge their responsibilities:

- Integrity and high ethical standards
- Sound judgement
- Ability and willingness to challenge and probe
- Strong interpersonal skills.

### Independent directors

An independent director is a director who has no relationship with the company, its related corporations, its 10% shareholders or its officers that could interfere, or be reasonably perceived to interfere, with the exercise of the director's independent business judgement with a view to the best interests of the company<sup>119</sup>. As such an independent director is also a non-executive director.

There should be a strong and independent element on the Board, which is able to exercise objective judgement on corporate affairs independently, in particular, from management and shareholders<sup>120</sup>.

Independent directors should make up at least one-third of the Board<sup>121</sup>. And at least half of the Board should comprise independent directors where the Chairman of the Board and CEO are the same person or immediate family members (immediate family members defined by SGX LR as the person's spouse, child, adopted child, step-child, brother, sister and parent), or is part of the management team and is not independent<sup>122</sup>. In such circumstances, a lead independent director could be appointed as a Board member to ensure a balance in the Board composition is attained<sup>123</sup>. The role of the lead independent also includes leading meetings with all independent directors (without the presence of non-independent directors) and any feedback, should be provided to the Chairman after such meetings<sup>124</sup>.

Each director's independence should be disclosed in the company's annual report<sup>125</sup>. The NC should determine annually whether the director is independent in character and judgment and if there are relationships that could impair or appear to affect the director's judgment<sup>126</sup>. Any such relationships should be disclosed including the following:

- a. A director being employed by the company or any of its related corporations for the current or any of the past three financial years

<sup>116</sup> CG Code Guideline 2.7

<sup>117</sup> CG Code Guideline 2.8

<sup>118</sup> Higgs, D., Review of the Role and Effectiveness of Non-executive Directors, Department of Trade and Industry (UK) Jan 2003, p 29 at para A.6.12 – [www.ecgi.org](http://www.ecgi.org)

<sup>119</sup> CG Code Guideline 2.3

<sup>120</sup> CG Code Principle 2

<sup>121</sup> CG Code Guideline 2.1

<sup>122</sup> CG Code Guideline 2.2

<sup>123</sup> CG Code Guideline 3.3

<sup>124</sup> CG Code Guideline 3.4

<sup>125</sup> CG Code Guideline 2.3

<sup>126</sup> CG Code Guideline 2.3 & 4.3

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### ► 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

- b. A director who has an immediate family member who is, or has been in any of the past three financial years, employed by the company or any of its related corporations and whose remuneration is determined by the remuneration committee
- c. A director, or an immediate family member, accepting any significant compensation from the company or any of its related corporations for the provision of services, for the current or immediate past financial year, other than compensation for Board service
- d. A director:
  - (i) who, in the current or immediate past financial year, is or was; or
  - (ii) whose immediate family member, in the current or immediate past financial year, is or was, a 10% shareholder of, or a partner in (with 10% or more stake), or an executive officer of, or a director of, any organisation to which the company or any of its subsidiaries made, or from which the company or any of its subsidiaries received, significant payments or material services (which may include auditing, banking, consulting and legal services), in the current or immediate past financial year. As a guide, payments aggregated over any financial year in excess of S\$200,000 should generally be deemed significant
- e. A director who is a 10% shareholder or an immediate family member of a 10% shareholder of the company
- f. A director who is or has been directly associated with a 10% shareholder of the company, in the current or immediate past financial year.

The primary task of independent directors is to adopt an oversight role and to ensure that the corporate assets are used only for the company. This task includes<sup>127</sup>:

- Being familiar with the fundamentals of the business in which the company is operating and continues to be informed about the activities of the company
- Reviewing the accounts of the company and asking additional information where needed
- Acting as a check on proposed corporate strategy bearing in mind the economics of any potential transaction
- Regular attendance at Board meetings to monitor corporate affairs and governance
- Participating in the appointment, assessment and remuneration of directors.

The NC is tasked with the responsibility to determine the independence of a director on annual basis<sup>128</sup>. The Code further states that the independence of any director who has served on the Board beyond nine years from the date of the first appointment should be carefully deliberated in ascertaining independence and the need for fresh members on the Board<sup>129</sup>.

If the Chairman and CEO positions are combined, a lead independent director may also be appointed.

<sup>127</sup> The Statement of Good Practice SGP No.7/2007

<sup>128</sup> CG Code Guideline 2.3 & 4.3

<sup>129</sup> CG Code Guideline 2.4

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
- 06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Executive directors

Executive directors are paid employees of the company. They are usually members of the company's senior management team. The CEO may also be an executive director and in some cases, other senior executives may also be appointed to the Board. The advantage of having the executive directors on the Board is that they add value to the Board's decision making process through their knowledge of the company's business and industry.

Executives might also offer a valuable second opinion to the statements and recommendations of the CEO. A risk does exist that their loyalty to the CEO could conflict with their statutory duty as a director to act in the best interests of the company.

### Nominee directors

A nominee director is a person appointed to the Board of directors to represent the interests of a substantial shareholder, JV partner, investor or creditor. The right to appoint is contained in the Constitution and/or in contractual documents, such as the JV agreement.

Nominee directors are bound by the same duty as other directors. Whilst a nominee cannot favour the nominator's interests over that of the company, they can consider the interests of the nominator, so long as the nominee director ultimately acts for a proper purpose and in the best interests of the company. Where the interests of the nominator and the company diverge, the nominee should be abstained from the decision making process. A nominee director must not divulge to the nominator information obtained from the company in the nominee's capacity as a director if there is a conflict between the

interests of the company and the nominator. The Act allows a nominee director to divulge information to his appointer only if he fulfils the following conditions:

- He must declare at a meeting of directors the name and office or position held by the person whom the information is to be disclosed to and particulars of such information<sup>130</sup>
- The director is first authorised by the Board of directors to make the disclosure<sup>131</sup>
- The disclosure will not be likely to prejudice the company<sup>132</sup>.

The nominee must either discharge their duty to the company and not to the nominator, or resign from the company's Board should there be any conflict of interest situations.

### Alternate directors

Where directors find themselves unable to attend all Board meetings or otherwise fulfil their Board commitments, an 'alternate' director can be appointed.

An alternate director is a full director and officer of the company himself in the eyes of the law and owes the same fiduciary duties and is subject to the same liabilities to the company. The right to appoint alternate directors would have to be provided for in the Constitution of the company. The notice appointing the alternate director should set out and be clear as to the terms of the alternate's appointment, powers, the circumstances they are to be exercised, any restrictions on authority, the scope of responsibilities, obligations, remuneration and benefits.

<sup>130</sup> CA Section 158(3)(a)

<sup>131</sup> CA Section 158(3)(b)

<sup>132</sup> CA Section 158(3)(c)



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
- 06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

The appointment of alternate directors is not encouraged although an alternate director has essentially the same powers, duties and liabilities as the director who appointed them. However, there could be exceptional circumstances (medical emergency or overseas leave) that justify the appointment of an alternate director. Prior to the appointment of the alternate director, the NC can assist the Board to review the reasons for such an appointment and to recommend the appointment of the alternate after reviewing the person's independence, credentials and familiarity with the company's affairs<sup>133</sup>.

The Board should ensure that the terms of the appointment of an alternate director clearly set out:

- the duration of the appointment
- the conditions under which the directorship may be revoked
- if the alternate director is permitted to attend all Board meetings
- if there is an entitlement to speak and/or vote and to receive all Board papers and other communications.

It is critical that the delegation be made for a specified timeframe. If the absence of the principal director is permanent or for a significantly extended timeframe, the absent director should consider stepping down and allow the NC to appoint a replacement director, rather than have an alternate take his place on a prolonged basis. If a principal director is unable to commit and dedicate sufficient time and attention to the affairs of the company, appointing an alternate is no substitute to the principal director's obligation to contribute effectively and demonstrate commitment to his role as a director.

In general, since independent directors are appointed to exercise objective judgement on corporate affairs independently from management and are chosen for their specific competence, expertise and experience, one would not ordinarily expect independent directors to appoint alternates to stand in for them. However, on the other hand, one should also take into consideration that the alternate director could be a potential candidate being assessed for appointment to the Board in his own right and/ or for succession purposes.

### Chairman's role

If the Board sets the tone for the entire company, then the Chairman sets the tone for the Board. The Chairman leads by example, displaying the utmost professionalism and engaging in conduct that is beyond reproach. In this sense, it is difficult to imagine a well-performing Board without an effective Chairman.

There should be clear division of responsibilities between the leadership of the Board and the executives responsible for managing the company's business. No one individual should represent a considerable concentration of power<sup>134</sup>.

It further states that the Chairman and the CEO should in principle be separate persons, to ensure an appropriate balance of power, increased accountability and greater capacity of the Board for independent decision making. The division of responsibilities between the Chairman and the CEO should be clearly established, set out in writing and agreed by the Board. In addition, the Board should disclose the relationship between the Chairman and the CEO if they are immediate family members<sup>135</sup>.

<sup>133</sup> CG Code Guideline 4.5

<sup>134</sup> CG Code Principle 3

<sup>135</sup> CG Code Guideline 3.1

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### ► 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

The responsibilities of the Chairman include<sup>136</sup>:

- Leading the Board to ensure its effectiveness on all aspects of its role
- Setting the agenda and ensuring that adequate time is available for discussion of all agenda items, in particular strategic issues
- Promoting a culture of openness and debate at the Board
- Ensuring that the directors receive complete, adequate and timely information
- Ensuring effective communication with shareholders
- Encouraging constructive relations within the Board and between the Board and management
- Facilitating the effective contribution of non-executive directors in particular
- Promoting high standards of corporate governance.

It is relatively common in Singapore for the Chairman to be the CEO as well since the majority of the listed companies were historically family run businesses<sup>137</sup>.

The Chairman may be exposed to 'additional liability' where circumstances may arise that they are a recipient and 'gatekeeper' of information that may not be available to other directors. It is paramount to ensure that any significant performance shortcomings attributed to the CEO are brought to the Board's attention and that the Chairman resists any complicity with the CEO to hold back information.

In addition, the Chairman must not prevent the CEO from raising issues with the Board, nor should the Chairman fail to raise any matter that would reasonably be judged worthy of the Board's consideration.

<sup>136</sup> CG Code Guideline 3.2

<sup>137</sup> Survey, NUS Business School Centre for the Governance, Institutions and Organisations, 2012

Given the significance of the Chairman's role, Boards should give careful attention to the election of a Chairman. The common practice of electing a Chairman according to a notion of seniority should not be the default position. The role should be filled by the candidate best able to fulfil the duties referred to above.

### Lead independent director

The recommendation in the Code provides that where the Chairman is not independent, it may be beneficial to consider the appointment of a 'lead independent director'. Appointment of the lead independent director is recommended if the Chairman and CEO positions are combined; the Chairman and the CEO are immediate family members; the Chairman is part of the management team; or the Chairman is not an independent director<sup>138</sup>.

The specific responsibilities of a lead director will vary among companies, but may include:

- being available to shareholders where they have concerns and for which contact through the normal channels has failed or is inappropriate
- acting as an intermediary between independent directors and the CEO, but not impeding opportunities for other directors to build a constructive relationship with the CEO
- setting the agenda and briefing the CEO on issues arising from those sessions
- collaborating with the Chairman/CEO in the preparation of the Board agenda and supporting papers

<sup>138</sup> CG Code Guideline 3.3

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### ► 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

- acting as a sounding board for the CEO in issues where the CEO wants to 'test the waters' prior to raising an issue with the full Board
- leading the appraisal of the Chairman/CEO.

The lead director is usually appointed by independent directors only and the company's former CEO should not be appointed as lead director.

### Company Secretary

Public companies are required to appoint a properly qualified person as a Company Secretary.

Company Secretaries are officers of a company and have certain responsibilities to fulfil and essentially have the same legal duties and obligations as directors<sup>139</sup>. The Company Secretary plays an important role within the corporate Board and the company and has wide ranging responsibilities as a senior corporate officer, serving as the focal point for communication with the Board of directors, senior management and the company's stakeholders. The role has increasingly become more important and is often seen as key advisor to the Board in advising administration and governance of important corporate matters. Directors should have separate and independent access to the Company Secretary<sup>140</sup>.

The Singapore Association of the Institute of Chartered Secretaries and Administrators (SAICSA)'s good governance guides provide details of the core duties of a Company Secretary, including having oversight over corporate governance matters, director/ officer/ shareholder matters and compliance/ regulatory matters.

Specifically:

- Advisor to the Board - advises and assists the Board with respect to their duties and responsibilities as directors, compliance with their obligations under the Act and SGX requirements and issues on corporate governance. Company Secretaries also act as a communication and information channel to executive, non-executive directors and management
- Controller of management functions - ensure that the Board's decisions are properly implemented and communicated by assisting in the implementation of corporate strategies and policies
- Corporate governance and compliance officer - ensure proper compliance with all relevant statutory and regulatory requirements
- Corporate communications - communicate with the stakeholders of the company as appropriate.

Additional principles to be applied to the Company Secretary role include<sup>141</sup>:

- Role should be clearly defined and should include the responsibility to ensure that all Board procedures are adhered to and compliance with all applicable rules
- Has a direct reporting line to the Chairman on all relevant matters relating to the Board. Attendance is required at all Board meetings.

Appointment and removal of the Company Secretary should be a matter for the Board as a whole<sup>142</sup>.

<sup>139</sup> CA Section 4(1)

<sup>140</sup> CG Code Guideline 6.3

<sup>141</sup> CG Code Guideline 6.3

<sup>142</sup> CG Code Guideline 6.4

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
- 07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

# 7. Insightful Strategy

Boards are responsible for ensuring the company is sufficiently agile to respond to changes in the business and economic environment and able to take advantage of emerging opportunities.

## Questions that company Directors should ask

- |  |   |
|--|---|
| 1. Are there annual strategic planning day(s) with Board attendance to discuss and approve the strategic objectives?   | 6. Has the Board and management defined shareholder value and how it is measured?   |
| 2. Does the Board drive management to develop a business model that provides the organisation with a competitive advantage?  | 7. Does the Board challenge and question management to achieve better strategy formulation?   |
| 3. Are different strategic options considered prior to a final decision being made by the Board?   | 8. Does management periodically provide the Board with performance benchmarks against the published figures of industry peers?        |
| 4. Does the Board have a well-defined process in place to monitor the quality of management's strategic execution, in terms of agreed strategic objectives and performance measures? | 9. Are the strategic options presented by management based on robust and thorough analysis using established tools and methodologies? |
| 5. For major projects, does management provide an in-depth business case which is independently verified?  | 10. Are post implementation reviews completed for all major projects?   |

## Red flags

- |  |   |
|--|---|
| ► The Board accepts management's strategy without in-depth probing or questioning          | ► Risks inherent in the strategy are not identified or managed        |
| ► The Board does not fully understand the nature and implications of the proposed strategy | ► Mechanisms for measuring shareholder value are not fully understood |
| ► The external environment is not fully considered in strategy development                 | ► Board meetings are not strategically focused                        |
| ► Not all directors attend the meeting where strategy is discussed and approved            | ► Too much emphasis is placed on financial performance measures       |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
- 07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Corporate strategy

Good corporate governance is about performance as well as conformance. The performance dimension of a Board's role focuses on business strategy and the pursuit of shareholder value.

The nature and extent of the Board's participation in strategy depends on the company's size, industry and particular circumstances. It is, however, essential that cooperative and interactive strategic planning processes are instituted which enable Boards and management to:

- Make, review and assess strategic decisions
- Understand the key drivers of company performance
- Align the company's strategy, operations and external environment
- Understand potential risks and incorporate risk management into strategic decision-making.

### Defining the Board's role in strategy

Boards are increasingly expected to play a leading role in developing, communicating and assessing corporate strategy. Regulators such as SGX, ACRA and MAS and other professional bodies have urged Boards to be more strategic, focusing on future performance, as well as compliance. Many directors believe strategy to be their most important sphere of activity, with their input having a significant influence on company performance.

Directors may often struggle to make a meaningful impact on the strategy process. This can occur for a number of reasons, including:

- Limited knowledge of the company's operating context

- Time constraints
- Board time being taken up with compliance issues
- Executives being unwilling to incorporate director input
- Not having a forum for participation (such as a specific strategic planning workshop).

As a result, some Boards may find they are side-lined in the strategy development process, being confined to merely approving or rejecting proposals. Reviewing, adding value to and approving the strategy are crucial to the Board's governance role. Boards need to be seen by management as a strategic resource that contributes to superior company performance. Through the Board's unique position, directors can contribute by providing:

- Market information and industry trends
- Experience and expertise accumulated during their professional careers
- New perspectives and fresh ideas
- An independent and objective viewpoint.

These strengths, combined with management's in-depth company knowledge and experience, mean that collaborative decision-making often leads to better strategy. Directors are more likely to add value to the strategy process if they possess a strong understanding of the company and its environment, have a strong, meaningful working relationship with each other as well as the management team, and are able to communicate and exchange information.



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
- 07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Understanding shareholder value

The Board and management must ensure that all strategic initiatives are designed to enhance shareholder value, but with appropriate consideration given to other relevant stakeholders. Shareholders define value from a different perspective to the company. To shareholders, value may be simply the dividends or cash equivalents they receive, plus the increase (or decrease) in the market value of their shareholdings over the life of their investment. Companies require more objective measures of shareholder value that are independent of the volatility

and ambiguity of market valuations. It is important for Boards to define and measure shareholder value. This definition will guide decision-making at all levels of the organisation.

There are two broad approaches for measuring shareholder value:

- Traditional – based on conventional financial accounting measures
- Net value – seeks to remove distortions and claims to identify movements in net shareholder value.

| Traditional                         | Net Value                              |
|-------------------------------------|--|
| Net income/net profit               | Cash flow return on investment (CFRoI) |
| Earnings per share (EPS)            | Market value added (MVA)               |
| Return on equity (RoE)              | Total shareholder return (TSR)         |
| Return on assets (RoA)              | Total business return (TBR)            |
| Return on net assets (RoNA)         | Shareholder value added (SVA)          |
| Return on capital employed (RoCE)   | Cash value added (CVA)                 |
| Net tangible assets per share (NTA) |  |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
- 07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Sustainable competitive advantage

The fundamental aim of corporate strategy is to provide an organisation with sustainable competitive advantage. This refers to the unique value-creating processes that set an organisation apart from its competitors. Sources of competitive advantage may include:

- Use of a leading edge business model
- Innovation
- Effective use of assets and resources, such as patents and other intellectual property, corporate reputation and physical locations
- Dynamic product lines
- The collective skills and experience of the executive and management team
- A lock on the market or customer base
- Strong focus and differentiation.

Most competitive advantages are short-lived because environments change rapidly. Creating sustainable competitive advantage over the long-term necessitates that companies be flexible and responsive. In fact, organisational agility and the ability to re-deploy organisational resources to take advantage of opportunities can be a sustainable competitive advantage in itself.

### Thinking strategically

An effective, well-articulated, strategic plan is critical for organisational success - it presents a vision for the future and a roadmap for how the company will get there. Developing such a strategy is the joint responsibility of the Board and management.

Boards should develop a culture of strategic thinking that can be assisted by:

- Creating a climate where strategic thinking is a valued activity
- Challenging and evaluating the processes for developing strategy, not just the strategies themselves
- Upholding high expectations for strategic plans
- Setting aside adequate time and resources to discuss strategy in a meaningful way
- Establishing methodologies, tools and policies for strategic decision-making and monitoring management adherence to them
- Ensuring that all company decisions align with the strategy.

### Stakeholder involvement in strategic planning

A critical step in the strategic planning process is engaging with key stakeholders. A company's stakeholders are those groups who affect and/or are affected by the company and its activities such as investors, lenders, analysts, employees and customers. In leading organisations, stakeholder engagement has migrated from an optional consideration to an integral part of the business strategy.

Boards face ongoing scrutiny and increasingly high expectations from stakeholders. As part of their responsibility for governance oversight, directors need to identify and understand the expectations of the company's stakeholders, which may vary across industries and are continually changing.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
- 07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

The CG Code suggests that the Board's role is to set the company's values and standards and consider that the obligations to shareholders and stakeholders are met and understood<sup>143</sup>. It is considered good practice to incorporate stakeholder views into the strategy development process, whether directly through consultation with stakeholder representatives, or by indirectly acknowledging their goals when generating strategy. Stakeholders bring expert advice or represent the interests of groups that can have a major effect on the success of the strategy. A diverse range of views and ideas can lead to more innovative problem solving. There should also be enhanced communication and trust, leading to mutual understanding and collaboration, potentially reducing legal and reputational risks and associated costs.

### Strategic risk

Boards must identify, assess and manage the risks inherent in any strategic plan. Strategic plans often do not achieve their desired aims, are poorly executed, or fail to keep pace with changes to the business environment.

Directors have a duty to satisfy themselves that an effective strategic risk management plan is in place and is being followed. Such plans seek to:

- Identify and evaluate strategic risks
- Consider emerging risks and trends
- Measure what is happening
- Prepare for, and take appropriate corrective action.

Boards must try to balance both short and long-term strategic risk. Strategic risk increases as the time horizon expands – the longer the timeframe, the more unpredictable it becomes, and thus the more

sophisticated the organisation's risk management capabilities need to be. Many organisations develop scenarios that deal with a variety of alternatives to mitigate this problem. Risk management is an increasingly vital part of organisational accountability and strategic decision-making.

### Strategy review

Strategy needs to be continually reviewed. It is the Board's responsibility to conduct a thorough analysis of current strategy and progress towards the agreed objectives, and to evaluate company performance in light of these objectives. This is a key part of the Board's monitoring role and should be completed without interference from management. A Board will normally review strategic direction at least annually. Strategies should also be subject to reviews to ensure that they remain appropriate to the organisation's needs. There is a danger that organisations become complacent in their strategy, making incremental adjustments whilst their environments continue to change rapidly. More agile competitors will quickly overtake companies that merely react to the environment, rather than challenging, questioning, and even influencing it.

In addition, Boards need to be vigilant in assessing company performance in achieving the strategy. Periodic reporting from management (such as a quarterly report card incorporating exception reporting) can help the Board quickly come to terms with what is not working and why.

It is important that the Board receives the appropriate facts and information to make an accurate assessment. Financial and operational reports are a good starting point, but the Board also requires non-financial performance indicators. These may include indicators of customer

143 CG Code Guideline 1.1(e)

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### ► 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

satisfaction, employee engagement, WH&S and community involvement. The Board is there to look objectively at company strategy and make the tough decision to change a company's course when it is no longer viable.

Rather than trying to predict the future, the Board can ensure that the organisation's capabilities and resources are sufficient to manage uncertainty and that strategic plans are flexible. In-built flexibility is promoted by:

- Scanning the environment constantly and keeping abreast of changes that could materially affect the achievement of strategic objectives
- Exploring how environmental shifts will impact on strategy
- Inviting subject experts to address the Board and senior management
- Ensuring accurate and timely information reaches the Board and is discussed candidly by directors and managers scheduling 'break-out' sessions to allow the Board to challenge the current strategy.

### Using the balanced scorecard

The balanced scorecard method is used by many companies globally as a better practice approach to setting performance measures and subsequently measuring actual performance. The idea of a balanced scorecard arises from the fact that financial measures are the end result of a range of other activities and processes taking place in companies. To increase sales, cut costs, lift

margins, raise profits and improve return on investment, companies must do things such as engage in activities, processes, programs and projects. Directors must get behind the financials to discover these value drivers. They must learn to measure value drivers if they are to manage them.

The balanced scorecard approach recommends that Boards view their business from many perspectives.

- Financial perspective – how does our performance look to shareholders? Are we adding value?
- Customer perspective – how do customers see us?
- Internal business perspective – what must we excel at?
- Innovation and learning perspective – can we continue to innovate and create value?
- Community and environment – how do we meet all stakeholder expectations?

Using a balanced scorecard approach, companies set themselves goals or business objectives for each perspective. They then select the measures that best calculate progress in achieving these goals. These goals and measures should be geared to the circumstances of individual companies.

The balanced scorecard provides a performance information framework that allows companies to evaluate the effectiveness of their strategy. The balanced scorecard methodology has been promoted mainly as a management process, but it makes an excellent reporting framework for company Boards.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
- 08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

# 8. Risk Management and Internal Controls

Ultimate responsibility for risk lies with the Board. Consequently, risk management and internal controls are a focus of the Board and executive management.

## Questions that company Directors should ask

- |  |   |
|--|---|
| 1. Are the relevant roles and accountabilities for governance, risk and compliance properly formalised and documented? | 4. Has the Board approved the risk appetite/ tolerance levels for the company?                    |
| 2. Are there early warning systems in place to alert the Board and senior management to emerging risks?                | 5. Does the Board challenge the risk approach, risk reporting and management plans?               |
| 3. Are the right risks being identified, assessed and managed?   | 6. Does the Board provide oversight on plans for crisis management and business continuity?       |
|  | 7. Is the Board establishing the 'tone at the top' to reinforce and promote a risk aware culture? |

## Red flags

- |  |   |
|--|---|
| ► Risk management is not connected to corporate strategy                     | ► Risk is considered in isolation from strategic planning and/ or major decision-making in the organisation       |
| ► Leadership from the top is lacking   | ► Risks identified are generic and do not appear to change significantly over time                                |
| ► Risk management is positioned as a compliance and backroom exercise        | ► Risks and mitigating actions are not regularly reviewed and prioritised to be implemented                       |
| ► Risk reporting and risk management plans are not challenged at Board level | ► Mitigating actions are often overdue  |
| ► A healthy risk culture is not embedded throughout the organisation         | ► There is little guidance or explanation about how the risk, internal control and assurance framework are linked |



## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### ► 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

### Singapore context

Directors should be aware of the key requirements that specify responsibilities and actions relating to risk management and internal controls. The key requirements are found in the following instruments:

- SGX Listing Rule 1207 (10) and Practice Note 12.2
- Singapore CG Code 2012 (predominantly Principle 11)

- Guidelines on Corporate Governance for Financial Holding Companies, Banks, Direct Insurers, Reinsurers and Captive Insurers (2013) [Singapore FI CG Code].

These requirements are supported by the following key guidance documents:

- Guidebook for Audit Committees in Singapore (Second Edition) [Guidebook for ACs]
- Board Risk Committee Guide (BRC Guidebook).

### Singapore risk governance requirements

Directors are required to understand the key requirements regarding risk governance. The table below highlights the key requirements (particularly in relation to disclosures):

|                          | SGX LR 1207(10) | Singapore CG Code 2012 |
|--------------------------|-----------------|------------------------|
| <b>Risk Management</b>   |                 |                        |
| Adequacy                 |                 | √                      |
| Effectiveness            |                 | √                      |
| <b>Internal Controls</b> |                 |                        |
| Adequacy                 | √               | √                      |
| Effectiveness            |                 | √                      |

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### ► 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

The Board should ensure that management maintains an adequate and effective system of risk management and internal controls to safeguard shareholders' interests and the company's assets. It should also determine the nature and extent of the significant risks which it is willing to take in achieving its strategic objectives<sup>144</sup>. Key risk management requirements are presented below:

- The Board should determine the company's levels of risk tolerance and risk policies, and advise management in the design, implementation and monitoring of the risk management and internal control systems<sup>145</sup>
- The Board should, at least annually, review the adequacy and effectiveness of the company's risk management and internal control systems, including financial, operational, compliance and information technology controls. Such review can be carried out internally or with the assistance of any competent third parties<sup>146</sup>
- The Board should comment on the adequacy and effectiveness of the internal controls, including financial, operational, compliance and information technology controls, and risk management systems, in the company's annual report. The Board's commentary should include information needed by stakeholders to make an informed assessment of the company's internal control and risk management systems<sup>147</sup>. In addition, it should also comment in the company's annual report on whether it has received assurance from the CEO and the CFO<sup>148</sup>:

(a) That the financial records have been properly maintained and the financial statements give a true and fair view of the company's operations and finances; and

(b) Regarding the effectiveness of the company's risk management and internal control systems

- A separate Board Risk Committee or similar should be established to assist the Board in carrying out its responsibility of overseeing the company's risk management framework and policies<sup>149</sup>. Refer to Chapter 9 Board Committees where this is covered in more detail.

In addition, the Board, with the concurrence of the Audit Committee, is required to provide an opinion on the adequacy of the internal controls, addressing financial, operational and compliance risks<sup>150</sup>.

Although it is not mandatory for listed companies in Singapore to comply with principles in the Code, SGX Listing Rule 710 mandates the requirement to explain the reasons for non-compliance.

Guidance on key concepts relating to risk management, internal controls and assurance is provided in the Guidebook for ACs – Chapter 3 Risk Management and Internal Controls and Appendix C.4 and the BRC Guidebook.

<sup>144</sup> CG Code Principle 11

<sup>145</sup> CG Code Guideline 11.1

<sup>146</sup> CG Code Guideline 11.2

<sup>147</sup> CG Code Guideline 11.3

<sup>148</sup> CG Code Guideline 11.3

<sup>149</sup> CG Code Guideline 11.4

<sup>150</sup> SGX LR 1207 (10)

## Foreword

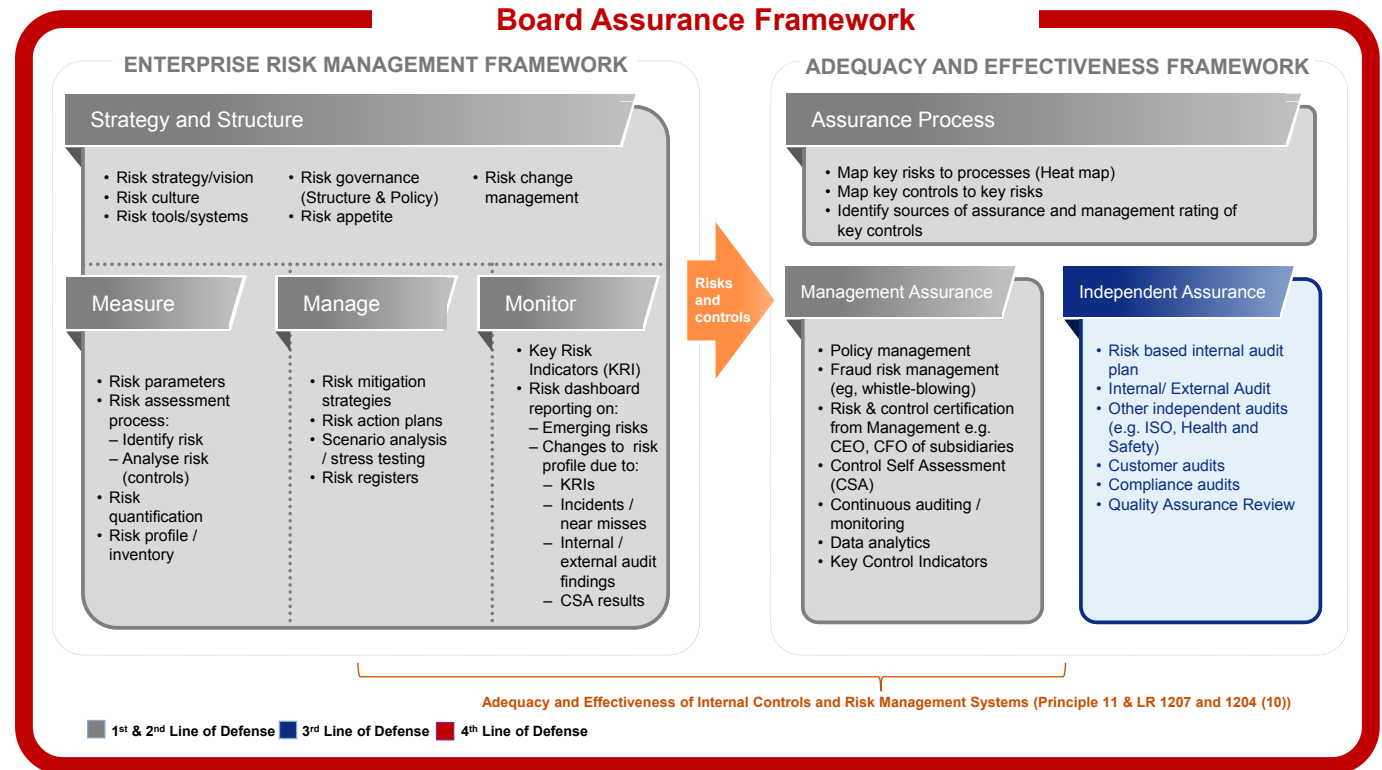
01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
- 08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Board Assurance Framework

To satisfy duties and obligations regarding risk management and internal controls, directors need to ensure there is a holistic Board Assurance Framework (BAF) in place that links enterprise risk management (ERM), internal controls and assurance activities. A BAF provides Boards with an overview of existing procedures in place to identify the key risks facing the business, how

they are being managed and what is being done to check that the controls are adequate and effective.

KPMG has developed a BAF to encourage Boards to consider what is needed to establish an ERM framework alongside an assurance framework. This allows the adequacy and effectiveness of risk management and internal controls to be assessed. For further guidance, refer to the Guidebook for ACs and BRC Guidebook.



Source: KPMG's Board Assurance Framework

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### ► 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

The ERM framework will be covered in detail in this chapter. The Adequacy and Effectiveness (Assurance) framework will be covered in detail in Chapter 10 Receiving Assurance.

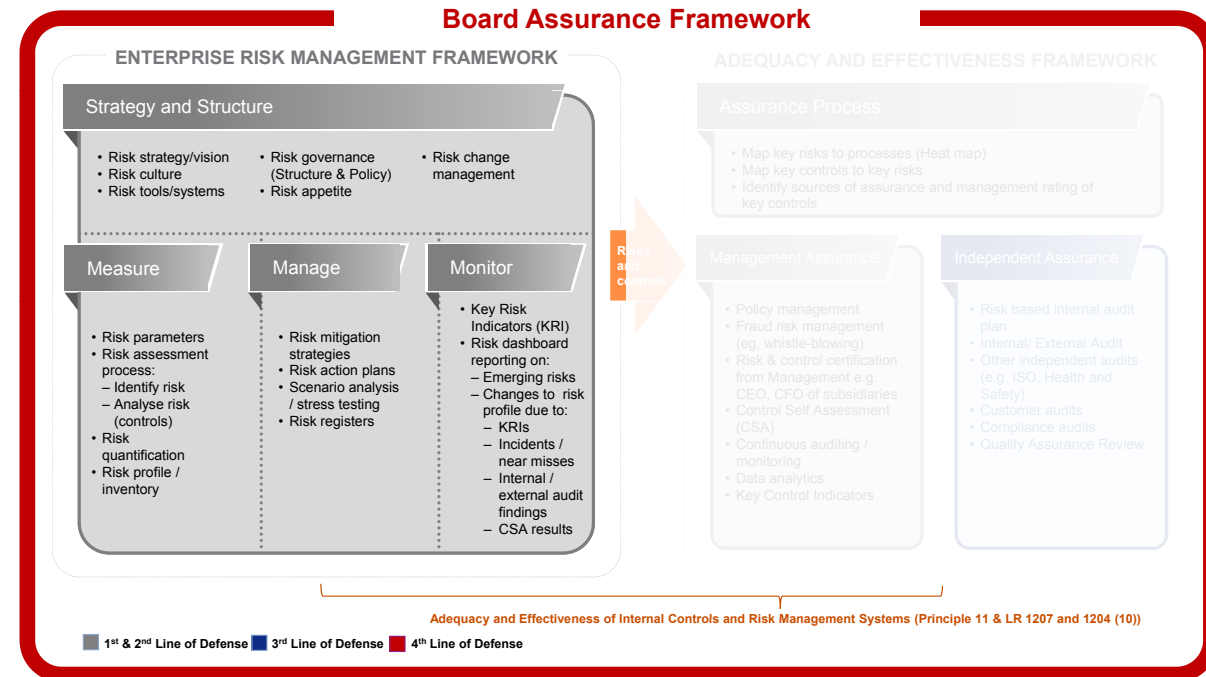
## Enterprise Risk Management

Given the nature, speed and velocity of risks facing companies, Boards need to ensure there is a structured approach that enables risks to be identified, assessed, prioritised, managed and communicated in a timely manner to key stakeholders.

To satisfy the Board's accountability for risk governance, they should ensure there is an adequate and effective ERM in place that is relevant for the nature, size, structure and complexity of their company.

There are a number of ERM and internal control frameworks commonly used by companies (e.g. the International Standards Organisation (ISO) 31000:2009 ERM Principles and Guidelines or the Committee of Sponsoring Organisations (COSO) ERM and Internal Control Frameworks). Further guidance and examples are provided in the Guidebook for ACs and the BRC Guidebook.

The BAF highlights the key elements of an ERM framework outlined below:



Source: KPMG's Board Assurance Framework

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
- 08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

While all aspects of the ERM framework need to be adequate and effective, the critical areas for Boards to focus on include:

### Risk and strategy

There is an intrinsic link between the development of strategy and the risks that threaten its achievement. Despite the benefits of integrating these two key processes, many organisations struggle to do this. However, integration is essential if organisations are to extract the most out of both strategic and risk management processes.

Experience suggests that organisations that make risk management an integral part of their strategy are more resilient in dealing with adverse events and uncertainty. Poor management of material business risks has been widely recognised as one of the key contributors to corporate failures during the global financial crisis. The global downturn has provided useful lessons that listed entities can draw on to improve risk management and risk disclosures to stakeholders.

### Risk appetite

The Board should determine the company's levels of risk tolerance<sup>151</sup>. Risk appetite is the amount and type of risk, on a broad level, that an organisation is willing to pursue or retain in the pursuit of its long-term strategic objectives<sup>152</sup>. Risk tolerance is defined as the boundaries of risk-taking outside of which the organisation is not prepared to venture in the pursuit of long term business objectives<sup>153</sup>. It will reflect the risk management philosophy and the organisation's capacity to take on risk. It will be based

on strategic objectives and stakeholder demands. The notion of risk appetite can add discipline and focus when responding to an uncertain and constantly shifting risk environment. A risk appetite statement can provide a decision-making framework for the strategic and operational handling of risk. A sample of risk appetite and tolerance statements can be found in Appendix 4F of the BRC Guidebook.

### Risk governance

Risk governance is the architecture within which risk management operates in a company. It defines the way in which a company undertakes risk management. It provides guidance for sound and informed decision-making and effective allocation of resources<sup>154</sup>.

Risk governance encompasses the overarching risk management structure to facilitate the management of risks across an organisation.

The common risk governance structures are outlined below<sup>155</sup>:

- Oversight by Audit Committee (AC)
- Oversight by Board Risk Committee (BRC)
- Oversight by Board.

Many ACs today have oversight responsibility for the company's ERM process, as well as other major risks facing the company – including financial, operational, cyber security, IT, legal and regulatory compliance.

Refer to Chapter 9 Board Committees and the Guidebook for ACs and BRC Guidebook where this is covered in more detail.

<sup>151</sup> CG Code Guideline 11.1

<sup>152</sup> BRC Guidebook, Appendix 4C

<sup>153</sup> BRC Guidebook, Appendix 4C

<sup>154</sup> BRC Guidebook, Section 4.5

<sup>155</sup> Guidebook for ACs, page 60



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
- 08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Risk management policy

The Board should determine the company's risk policies and oversee management in the design, implementation and monitoring of the risk management and internal control systems<sup>156</sup>.

Risk management policies should reflect the company's risk profile and should clearly describe all elements of the risk management and internal audit function. The policy should be an instrument to communicate the company's risk management approach and should include, at a minimum:

- a definition of 'risk' and 'risk management' relative to the organisation
- goals and strategies for risk management
- the organisation's risk appetite/tolerance
- how risk management targets will be measured
- accountabilities for risk management.

There should be formal policies and procedures in place for key risk areas, disciplines and reporting.

Refer to the BRC Guidebook section 4 for further information regarding risk management policies.

### Risk culture

Boards should not overlook the importance of embedding the right culture throughout the organisation, alongside any improvements in techniques and processes. For risk management to be effective:

- There is a need for openness throughout the organisation. This will enable management and staff to escalate concerns in a timely manner without fear. Good culture results in better judgement, which

reduces the reliance on process and provides greater comfort to the Board and management

- Boards need to lead by example and set the right tone at the top in order to influence the behaviour of management and staff. Thus, the leaders, in particular the Chairman and the CEO, should be seen to embody the values they espouse.

Some practices that may help create a risk-aware organisation and a common risk culture include:

- Establishing values statements and codes of conduct
- Communicating the Board vision, strategy, policy and responsibilities and reporting lines to all employees as well as stakeholders
- Developing training programmes for risk management
- Identifying and training "risk champions"
- Clear communication about any risks or practices for which there is zero tolerance
- Clear communication of the boundaries within which employees can operate
- Periodic risk reports to the Board and/or the appropriate Board committee
- Periodic discussions of risk and risk issues with management
- Clear allocation of responsibility for managing specific risks
- Developing a knowledge-sharing system
- Review and evaluation of performance against rewards.

156 CG Code Guideline 11.1

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
- 08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

The company's remuneration framework and policy should include a component on risk management. There must be alignment with the risk tolerance and overall risk strategy of the company to encourage the desired behaviour of staff. The Remuneration Committee should conduct periodic reviews of the framework to ensure relevance and consistency.

Refer to the BRC Guidebook section 4.6 for further information regarding risk culture.

### Crisis management

Companies should have crisis management plans in place. Such plans should include reference to the Board's role during a crisis and should be considered as part of a Board's risk management responsibility.

Boards should ensure that crisis management plans contain a robust communications element.

Without effective communication, companies may inflict additional damage on themselves including:

- Losing control of the communications process
- Allowing facts to be displaced by rumour and speculation
- Reputational harm
- Putting employee morale and trust at risk
- Alienating shareholders, customers, suppliers and other stakeholders.

### Business continuity

Planning for potential disaster scenarios is considered a crucial practice as all businesses face the risk of a serious event occurring that can damage the organisation's ability to continue operating.

Business continuity management focuses on an organisation's responsiveness to an organisational or external crisis that puts its ongoing operations at risk. The aim is to foster and develop preparedness for all types of events that may significantly affect an organisation and enable a company to respond and resume normal business operations after they occur.

The ultimate goal of business continuity is to develop a response to events to enable the organisation to maintain its most critical operations, and survive all but the most extreme forms of operational disruption. The key elements of effective business continuity planning are flexibility and simplicity.

A well-prepared organisation will be able to make the right decisions at the right time, based not on rigid instructions contained in a detailed manual, but on tried and tested alternative ways of working. These arrangements must:

- Be integrated into everyday business
- Look inside as well as outside the organisation
- Be understood by employees and stakeholders
- Be regularly and effectively tested to ensure they remain relevant.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
- 08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Enterprise-wide risk management framework – process

| Framework Element                  | Description   |
|------------------------------------|---|
| <b>Strategy and Structure</b>      |   |
| 9. Risk Strategy & Appetite        | Knowing what you aim for – Define ERM vision and strategy to support strategic objective and derive the best fit 'ERM target operating model'.  |
| 10. Risk Organisation & Governance | Setting and communicating the rules of the game – Define the risk management mandate, risk roles and responsibilities across the organisational levels and develop risk policy.                     |
| 11. People & Culture               | Educating and engaging people – Evaluating common and specific characteristics of risk culture to serve as an aiming point for ERM change programme.  |
| 12. Risk Data & Infrastructure     | Fostering data analytics – Use of technological enablers to document, monitor and report risk data and enable accurate risk assessment and performance evaluation.                                  |
| <b>Measure and Manage</b>          |   |
| 13. Risk Assessment                | Connecting the top with the bottom – Identify, evaluate and manage key strategic, financial, operational, compliance and information technology risks throughout the various organisational levels. |
| 14. Risk Techniques & Methods      | Getting tactical and technological – Apply appropriate qualitative and quantitative tools with 'forward looking' techniques designed for uncertain environments and proactive risk management.      |
| <b>Monitor</b>                     |   |
| 15. Risk Monitoring & Reporting    | Driving risk hindsight and foresight – Monitor and report significant risks from operations up to the Board.  |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
- 08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Organisational roles

#### *The Board*

As noted above, the Board is ultimately responsible for risk management. The Board:

- Approves the organisation's risk appetite as recommended by the audit (and/or risk) committee
- Must regularly review and approve the organisation's risk management policy, and maintain oversight of the policy
- Approves the risk management framework for the organisation
- Receives regular updates about key risks, changes in risks and emerging risks from the audit and risk committee
- Establishes Board sub-committees (audit and risk committee) and evaluates committee performance.

#### *Board Risk Committee*

The Board may establish a separate Board Risk Committee (BRC) to assist it in carrying out its responsibility of overseeing the company's risk management framework and policy<sup>157</sup>. A BRC is often an efficient mechanism for focusing the company on appropriate risk oversight, risk management and internal control. Although not a mandated requirement for listed companies (that are not deemed financial services institutions<sup>158</sup>), many companies have established BRCs, or have a combined audit and risk committee. For companies that do not possess a risk management committee

(e.g. in the case of smaller Boards where the same efficiencies may not necessarily be derived from a formal committee structure), Board processes should raise the issues that would otherwise be considered by a BRC.

Generally the BRC will have a key role in the governance of risk and compliance, including:

- Oversight of the risk management framework and its implementation
- Considering and challenging risk reporting
- Oversight of the compliance framework
- Considering and directing management's response to key risk issues.

Refer to Chapter 9 Board Committees and the BRC Guidebook where this is covered in more detail.

#### *Chief Risk Officer*

A number of businesses have appointed a chief risk officer (CRO) or risk manager. The existence of a CRO centralises risk management, but also brings several other benefits. One is to understand relationships between risks across separate business units that might not have been apparent before. This is increasingly important with the greater diversity and complexity of global businesses; risks that seem acceptable to an individual business unit may be inappropriate from the point of view of the enterprise as a whole. Using a comprehensive risk matrix, CROs can identify such linkages across the business and manage them more effectively.

<sup>157</sup> CG Code Principle 11.4

<sup>158</sup> Financial institutions are required to establish a BRC under the Singapore FI CG Code

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
- 08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

Another important way CROs can benefit the business is by enabling the organisation to make decisions based on a better appreciation of the relationship between risk and reward. CROs are most effective when they provide the Board with a clear vision of where enterprise risks lie, help define a policy for distributing and offsetting those risks, and work to communicate that vision so that individual managers understand and support it. The CRO provides a framework for risk management, but it is for frontline managers and employees to determine the criteria for 'acceptable risks'.

### *Internal audit*

Internal audit plays a multifaceted role in ERM. The Institute of Internal Auditors notes that internal audit's core role in ERM is to provide objective assurance to the Board on the effectiveness of an organisation's ERM activities to help ensure key business risks are being managed appropriately and that the system of internal control is operating effectively. In addition, many companies look to internal audit to support strategic business objectives. That effort extends to ERM activities such as:

- Risk identification and prioritisation
- Alignment of people, processes and systems with the business strategy

- Definitions of key performance indicators
- Analysis and quantification of risk factors in new business ventures and strategies
- Understanding the shared risks among various projects and initiatives.

Internal audit's role, its knowledge of the organisation's key risks, and its enterprise-wide view enable it to bring an important perspective and discipline to an ERM effort.

Forward-thinking organisations are those that do not view compliance risk management as a cost of doing business, but rather as a strategic investment critical to business resilience, efficiency and success.

Strategic compliance risk management requires customised design and development of compliance arrangements. A one-size-fits-all approach to the design of compliance arrangements is not always appropriate or practical.

Refer to Chapter 10 Receiving Assurance for further information on the role of Internal Audit.



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
- 09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

# 9. Board Committees

As managing and controlling companies becomes more complex, the Board can enhance its oversight function and remain accountable to shareholders by establishing Board committees to assist directors to better perform their duties and discharge their responsibilities.

## Questions that company Directors should ask

- |  |  |
|--|--|
| 1. Does the Board have an appropriate Board committee structure in place?  | 5. Does the Board constructively challenge information provided by a Board committee, even when endorsed by 'experts'? |
| 2. Are there terms of reference for each Board committee and are the charters approved by the Board and reviewed annually? | 6. Does the Board receive from each committee reports that are complete, concise, timely, and accurate?                |
| 3. Do Board committees have the right balance of non-executive and/or independent directors?                               | 7. Is the Board informed of any issue in which committee members are not in full agreement?                            |
| 4. Do all Board committees have the expertise and experience to properly advise the full Board?                            | 8. Is there a robust process to evaluate the Chairman of the Board and of each committee?                              |

## Red flags

- |   |  |
|---|--|
| ► Board committees lack terms of reference or charters  | ► There is no robust process in determining independence of directors or committee members                                       |
| ► Certain committees are not resourced with appropriately skilled people  | ► The Audit Committee meets only when required by internal or external auditors  |
| ► The Board committees are not meeting regularly enough to address issues on hand   | ► The Audit Committee has little to do with assessing internal control systems and coordinating with the internal audit function |
| ► Committee meetings are not minuted or the minutes are not distributed timely to members   | ► Similar sized companies or competitors have established additional committees that the company is yet to establish             |
| ► The Audit, Nomination or Remuneration committee involve mostly executive directors due to the unavailability of independent directors |  |

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### ► 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

The Board may delegate the authority to make decisions to any Board committee, but it must do so without relinquishing its responsibility and such delegation should be disclosed<sup>159</sup>.

Board committees should be chaired by an independent director and should comprise a majority of independent members. The Board and its Board committees should consist of directors who as a group provide an appropriate balance and diversity of skills, experience, gender and knowledge of the company. They should also provide core competencies such as accounting or finance, business or management experience, industry knowledge, strategic planning experience and customer-based experience or knowledge<sup>160</sup>.

The advantages of setting up Board committees include:

- Improving efficiency and effectiveness of directors to perform Board work with the amount of time available
- Achieving greater focus on matters needing to be addressed
- Sending a positive signal to the shareholders that pertinent issues are being dealt with impartially by directors with the relevant experience and skill-sets
- Allowing independent directors to attain in-depth understanding of the business.

The most common Board committees in Singapore are:

- Nominating Committee
- Remuneration Committee
- Audit Committee
- Board Risk Committee.

There is an emerging trend for the Board to establish an Audit Committee with a separate Board Risk Committee, particularly among large companies and within the financial services sector. According to the KPMG-SGX CG disclosure study conducted in 2016, out of the 545 mainboard listed companies, 32% of the large-cap companies have formed BRCs, compared to just 15% of the mid-cap companies and 5% of the small-cap companies.<sup>161</sup>

Other types of committees may also be set up if necessary, taking into account size and nature of the company's business and/or regulatory requirements. These Board committees may include a Finance and Investment Committee or a Special Purpose Committee.

The Board committees should adopt the same systematic planning and processes as the full Board, including:

- Setting up a Board committee charter with detailed description of roles and responsibilities
- Establishing an annual agenda
- Documenting matters being discussed and resolved.

Committees should report regularly to the Board through both a verbal report by the committee Chairman and a detailed report and/or committee minutes in the Board papers. They should also review their charters and membership at least annually and recommend any required changes to the full Board.

<sup>159</sup> CG Code Guideline 1.3

<sup>160</sup> CG Code Guideline 2.6

<sup>161</sup> KPMG-SGX CG disclosure study 2015

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
- 09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

Having Board committees presents its own set of challenges including:

- Having to ensure that the committee comprise directors with the appropriate expertise and resources to provide the full Board with good advice
- The legal question of whether a higher standard of care should apply to the directors on the Board committee, who are vested with the responsibility of investigating particular issues and making recommendations to the full Board.

### Committee charter

The starting point for any Board committee is a formal charter or terms of reference. The charter helps the committee members to understand their duties and responsibilities and how these can be reconciled with the expectations of the full Board and the organisation's stakeholders.

A typical committee charter covers the:

- Committee purpose, responsibilities and duties
- Authority and accountability of the committee (including delegations by the Board)
- Committee structure and terms of appointment for the Chairman and members
- Meeting requirements and procedures (e.g. frequency of meetings, quorum, voting and minutes)
- Access to company personnel and independent external advisers
- Members' skills and experience requirements
- Board reporting requirements
- Committee assessment process.

Committee charters should also be posted on the organisation's website with key features included in the

governance statement in the annual report in accordance with the Singapore CG Code.

In addition, the Board charter should be reviewed at least annually and any changes should be tabled to the full Board for approval.

### Committee annual agenda

An annual agenda provides the framework to manage the committee's time, resources, meeting frequency and the matters considered by the committee.

An effective annual agenda:

- Reflects the complete committee's roles and responsibilities
- Shows alignment with the Board annual agenda to ensure integration of the Board and its committees
- Provides a summary of the committee's key activities and follow up measures to achieve results
- Prevents meetings being 'crowded-out' by peripheral issues
- Ensures the committee's insights and expertise are fully utilised.

The annual agenda brings the committee charter to 'life' as it drives the committee's activities, agendas and information requirements. For more information, refer to the example Audit Committee annual agenda in Appendix 4.

The discussion on the annual agenda should encourage involvement of committee members concerning the nature and timing of agenda topics. The committee annual agenda also helps to determine non-committee members who should be invited (including management and external advisers) to meetings and identifies potential conflicts of interest.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
- 09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Committee induction framework

Over the past few years, the responsibilities of audit and Board committees have increased significantly. Committees will not be able to safeguard the interests of shareholders unless their committee members have the capability to challenge management. The Board committee members are also expected to have sound knowledge of financial requirements and regulations governing the areas impacting the company; where required, they should have access to seek independent advice from external consultants or advisors.

A formal induction framework for new committee members is essential and the induction framework should include provision of:

- Information package with key business documentation  
Information package could include committee charter, committee annual agenda, committee papers and minutes for the past 12 months, the resources utilised to undertake duties, details of regulatory or compliance framework matters in relation to the committee and disclosure of how the committee has discharged its responsibilities.
- Training sessions  
The company can organise a training session for the committee members, to guide the committee on protocols, effective meetings, roles and accountabilities, review and reporting requirements.
- Meetings with key business executives and external consultants/ advisors  
Meetings with key executives (CEO, CFO, general counsel, compliance officer) and external advisors (external auditor, internal auditor) could include discussion on main strategies, financial and operational dynamics.

### Committee meeting agenda and minutes

Each committee meeting agenda should be prepared with reference to the committee's charter and annual agenda. The meeting agenda should consider the content for discussion, time allocation to discuss each item and invitees relevant for the discussion or item.

The committee Chairman and Company Secretary should take responsibility for the content of the agenda. They may seek feedback from other committee members, the CEO and senior management. A good agenda is one that enhances the quality of the committee's discussion by focusing on those critical matters requiring careful deliberation.

The Company Secretary is usually tasked with the responsibility of maintaining a complete set of committee papers, including minutes of meetings, meeting agendas and supporting documents.

Committee draft minutes should be circulated to members after meetings and to all directors for information. Approval of minutes should be obtained at the next meeting of the committee.

### Committee size and composition

While the size of a committee varies according to the organisation, a sufficient number of members with the necessary knowledge and expertise should be present in any committee.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
- 09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

In determining the appropriate size for each committee, the following should be taken into account:

- Complexity and geographic diversity of the organisation
- Nature and extent of the Board committee's responsibilities
- Numbers needed to encourage robust and insightful debate
- Knowledge and experience required of committee members
- Minimum number of members to allow quorum.

The Audit, Nomination and Remuneration Committees should consist of at least three members, of whom majority should be independent directors<sup>162</sup>. In the case of the Audit Committee and Remuneration Committee, all members should consist only of non-executive directors and be chaired by an independent director<sup>163</sup>.

### Committee/Board interaction and reporting

The Board committees should provide complete, comprehensive and accurate reporting to the full Board on a periodic basis as ultimately the full Board is responsible for making decisions based on the recommendations of its committees.

It is therefore vital that the Board takes the following measures:

- Questions the committee Chairman and members when the committee report is being presented to obtain assurance that the information can be relied upon

- Challenges whether the organisation's culture is appropriate, including the 'tone at the top', from a control perspective
- Be informed of any issues on which committee members were not in total agreement
- Confirms that any external parties/ advisors have been effective in providing the required assurance.

### Committee evaluation

A formal annual assessment of the effectiveness of the Board committees is recommended<sup>164</sup>. In addition, the process of evaluating the performance of the Board committees should be disclosed in the company's annual report. If an external facilitator is engaged to perform the committee's performance evaluation, the company should also disclose whether the external party has any connection with the company or any of its directors<sup>165</sup>.

Individual assessments of committee chairmen should be undertaken regularly by the Chairman of the Board and by committee Chairmen for individual committee members.

The key areas that should be covered in the Board committee's assessment:

- Roles and responsibilities – focuses on understanding of structures, roles and authorities
- Practices – covers matters relating to decision making in meetings and access to information
- Performance – looks into whether the committee's objectives are achieved and performance monitoring processes

<sup>162</sup> CG Code Guidelines 4.1, 7.1 & 12.1

<sup>163</sup> CG Code Guidelines 4.1 & 12.1

<sup>164</sup> CG Code Principle 5

<sup>165</sup> CG Code Guideline 5.1



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
- 09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

- Culture – refers to robustness and openness to discussions amongst members
- Composition – refers to member's competencies and skillsets.

The assessment process typically is conducted using several methods, including:

- Completing a self-assessment survey or questionnaire
- Conducting interviews with committee members, as well as management and assurance providers. This could be conducted less frequently i.e. as and when the company seeks to obtain more insights into areas needing improvement
- A review of the quality, quantity and relevance of information coming to, and emanating from, the committee.

The assessment's outcome should be a report providing an objective, balanced evaluation of the committee's effectiveness and highlighting specific areas for improvement.

### Nominating Committee ("NC")

The Board should establish a NC to make recommendations to the Board on all Board appointments, with written terms of reference which clearly set out its authority and duties<sup>166</sup>. The Board should disclose in the company's annual report the names of the members of the NC and the key terms of reference of the NC, explaining its role and the authority delegated to it by the Board<sup>167</sup>.

The NC is tasked to make recommendations to the Board on relevant matters<sup>168</sup> relating to:

- a. Review of Board succession plans for directors, in particular, the Chairman and for the CEO
- b. Development of a process for evaluation of the performance of the Board, its Board committees and directors
- c. Review of training and professional development programs for the Board
- d. Appointment and re-appointment of directors.

In general, the NC should regularly:

- Review the structure, size and composition (including the skills, knowledge, experience and diversity) required of the Board and make recommendations to the Board with regard to any changes
- Before recommending a new appointment, evaluate the balance of skills, knowledge and experience on the Board. A description of the role and capabilities required for a particular appointment should be prepared. And upon appointment, directors should receive a formal letter of appointment setting out clearly what is expected of them in terms of time commitment, committee service and involvement outside Board meetings
- Consider progressive renewal of the Board and each director's competencies, commitment, contribution and performance (e.g. attendance, preparedness, participation and candour)
- All directors should be required to submit themselves for re-nomination and re-appointment at regular intervals and at least once every three years.

<sup>166</sup> CG Code Guideline 4.1

<sup>167</sup> CG Code Guideline 4.1

<sup>168</sup> CG Code Guideline 4.2

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### ► 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

- Give full consideration to succession planning for directors and other key executives
- Deploy a performance evaluation process to assess whether directors are spending sufficient time to fulfil their duties
- Review measurable objectives for the implementation of the Board's diversity policy and monitor progress towards the achievement of these objectives
- Assess the independence of non-executive directors  
If the NC considers that a director who has one or more of the relationships mentioned in Guideline 2.3 and 2.4 of the CG Code can be considered independent, the NC is required to provide its views to the Board for consideration. Conversely, the NC also has the discretion to consider that a director is not independent even if do not fall under the circumstances set forth in Guideline 2.3 or Guideline 2.4 of the CG Code, and should similarly discuss the rationale before the full Board for discussion.
- Review and monitor the training and continuous professional development of directors and senior management.

There should be a formal annual assessment of the effectiveness of the committee, its Chairman and individual members.

The Company Secretary of the company would usually provide support i.e. setting out agenda of meetings and take action on issues and matters arising from the meetings of the NC.

In order to put together and operate an effective NC, the following attributes are recommended to be in place<sup>169</sup>:

- i. Appropriate leadership, size and composition

The NC should be chaired by an independent director with strong leadership qualities. In addition, the NC should comprise at least three directors, majority of whom should be independent<sup>170</sup>.

It is not encouraged for the:

- Chairman to chair the NC due to concerns of over dominance; or
- CEO to be a member of the NC due to not being independent.

- ii. Clearly defined charter

The Board should clearly define and approve the NC's terms of reference, in accordance with the Constitution.

Refer to Nominating Committee Guide 2012, Page 16 and 17 (Extract 2 and 3) for suggested duties of a NC.

- iii. Regular and planned meetings

Greater duties demanded of the NC require meetings to be well-planned and held more frequently. The committee can set Board meeting agendas to cover matters to be discussed over several meetings. The agenda should cover review of:

- Terms of reference
- Size, structure, skill gaps, time commitment, competencies, independence of Board and its committees
- Board succession
- Induction and training for new and existing directors

<sup>169</sup> Nominating Committee Guide 2012 written by Associate Professor Mak Yuen Teen, of the NUS Business School together with Mr Irving Low, Head of Risk Consulting at KPMG Singapore

<sup>170</sup> CG Code Guideline 4.1

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### ► 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

- Search and nomination of new directors
  - Process and tools for evaluating Board, committees and individual directors
  - Results of assessments
  - Appointment of new directors
  - Recommendation for re-appointment of existing directors.
- iv. Clear discussion and documentation on key decisions
- Key issues have to be discussed in depth with demonstrable due care and diligence. Key decisions include matters such as reviewing directors' independence, nomination and selection process and disclosure of multiple directorships held by each director in its annual report. When a director has multiple Board representations, they must ensure that sufficient time and attention are given to the affairs of each company. The NC should decide if a director is able to and has adequately carried out his duties, taking into consideration the director's number of listed company Board representations and other principal commitments. The Board should determine the maximum number of listed company Board representations which any director may hold, and disclose this in the company's annual report<sup>171</sup>.

- v. Adequate access to resources and information
- The NC must have access to the company or Board secretary since the latter is familiar with regulations and other governing instruments of the company. The NC may also meet with the head of human resources on matters relating to succession planning of key senior executives and the competency framework. External consultants may also be engaged.
- vi. Balance continuity with renewal
- A director's independence should be re-assessed if they have served on the Board above 9 years<sup>172</sup>. However, it is important that the NC recognises the need to strike a balance between appointing a new director and re-electing an existing director, and the specific basis for retaining a long-standing director.
- vii. Assessment of the NC
- The NC is required to be assessed by the Board in discharging its responsibilities. Processes and tools adopted can be similar to those used to assess the performance of the Board, other committees and individual directors.

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### ► 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

#### viii. Reporting by the NC

The NC is required to report certain matters relating to its responsibilities. Refer to the table below for a summary of matters to be reported:

| No. | Reference in CG Code  | Guideline     |
|-----|---|---------------|
| 1.  | Any delegation of authority by the Board to the NC, to make decisions on certain Board matters  | Guideline 1.3 |
| 2.  | The number of meetings of the NC committees held in the year, as well as the attendance of every member at these meetings   | Guideline 1.4 |
| 3.  | The induction, orientation and training provided to new and existing directors  | Guideline 1.6 |
| 4.  | Identification of each director who is considered to be independent. Where the Board considers a director to be independent in spite of the existence of a relationship as stated in the CG Code that would otherwise render a director not to be independent, the nature of the director's relationship and the reasons for considering him as independent | Guideline 2.3 |
| 5.  | Where the Board considers an independent director, who has served on the Board for more than nine years from the date of his first appointment, to be independent, the reasons for considering him as independent.  | Guideline 2.4 |
| 6.  | Names of the members of the NC and the key terms of reference of the NC, explaining its role and the authority delegated to it by the Board   | Guideline 4.1 |
| 7.  | The maximum number of listed company Board representations which directors may hold   | Guideline 4.4 |
| 8.  | Process for the selection, appointment and re-appointment of new directors to the Board, including the search and nomination process  | Guideline 4.6 |
| 9.  | Key information regarding directors, including which directors are executive, non-executive or considered by the NC to be independent   | Guideline 4.7 |
| 10. | How assessment of the Board, its Board committees and each director has been conducted. If an external facilitator has been used, the Board should disclose whether the external facilitator has any other connection with the company or any of its directors. This assessment process should be disclosed.  | Guideline 5.1 |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
- 09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Remuneration Committee ("RC")

The RC is increasingly active in overseeing how directors and senior executives are compensated. There should be a formal and transparent procedure for developing policy on executive remuneration and for fixing the remuneration packages of individual directors<sup>173</sup>. No director should be involved in deciding his own remuneration. The RC is encouraged to also work alongside NC to effectively remunerate directors and key executives.

To avoid potential (actual or perceived) conflicts of interest, the RC should consist of entirely non-executive directors, a majority of whom, including the Chairman, should be independent directors<sup>174</sup>.

Similar to other Board committees, the RC should have proper terms of reference to include:

- Supporting the company in developing a remuneration framework for directors and executive management that cascades down to employees. The framework should be developed to meet these objectives:
  - Attract and retain talent
  - Align with shareholders' interests
  - Maintain internal equity
  - Achieve balance in the mix of fixed and variable components of remuneration for both annual and long term business performance
  - Attain company's desired culture
- Regularly reviewing the remuneration framework and providing recommendations for the Board to discuss
- Reviewing directors fees periodically

- Making decisions on hiring and termination of key executives
- Ensuring that contracts of service contain fair and reasonable termination clauses which are not overly generous.<sup>175</sup>

A key task of the RC is to monitor levels of remuneration across relevant industries, and the economy as a whole, in order to ensure that the company's remuneration policies are effective in attracting, retaining and motivating the people integral to its success.

In structuring long-term incentive awards (whether stock or cash-based) for executives, the RC should consider the company's performance over the years, relative shareholder returns, the value of similar awards to executives at comparable companies and what has been given in the past years to the executives.

### Audit Committee ("AC")

The Board is required to establish an AC with written terms of reference clearly setting out its authority and duties<sup>176</sup>.

Refer to [Appendix 3](#) for a sample of an Audit and Risk Committee Charter.

The AC should comprise at least three directors, the majority of whom including the AC Chairman should be independent. All of the members of the AC should be non-executive directors<sup>177</sup>. At least two members, including the AC Chairman, should have recent and relevant accounting or related financial management expertise or experience<sup>178</sup>.

173 CG Code Principle 7  
174 CG Code Guideline 7.1

175 CG Code Guideline 7.4  
176 CG Code Principle 12  
177 CG Code Guideline 12.1  
178 CG Code Guideline 12.2



## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### ► 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

The CA also requires the AC Chairman to be independent, with no involvement in any executive functions in the company or its related companies<sup>179</sup>. A non-executive Chairman of the Board would not normally assume the role of AC Chairman.

In addition, a former partner or director of the company's existing auditing firm or auditing corporation should not act as a member of the company's AC: (a) within a period of 12 months commencing on the date of his ceasing to be a partner of the auditing firm or director of the auditing corporation; and in any case (b) for as long as he has any financial interest in the auditing firm or auditing corporation<sup>180</sup>.

In 2014 KPMG surveyed 1,500 Audit Committee members in a number of countries.

Singapore Audit Committee Institute's Priorities for 2016<sup>184</sup>

Key findings are as follows:

- Regulation, uncertainty and volatility, and operational risk are top challenges today.
- The quality of information about cyber risk, technology and innovation, and global systemic risk is falling short.
- Leading indicators and non-financial drivers of long term performance are often elusive.
- The Audit Committee's job continues to grow more difficult.
- Most companies don't have a CFO succession plan in place.
- Internal audit should also be looking at risk management, IT, and operational risk – but may lack necessary skills and resources.

Key findings are as follows:

- Maintain (or regain) control of the committee's agenda
- Quality financial reporting starts with the CFO and finance organisation; maintaining a sharp focus on leadership, succession planning, and bench strength is critical
- Monitor fair value estimates, impairments and judgement impacting key assumptions underlying other critical accounting estimates
- Access the company's readiness for the new revenue recognition standard from the IASB and FASB, and for new country-by-country tax reporting
- Reinforce audit quality and set clear expectations for the external auditor
- Consider how the company's disclosures can better tell the company's story – and the Audit Committee's

179 CA Section 201B(3)

180 CG Code Guideline 12.9

181 KPMG in Singapore: Adaptation of KPMG's Global Audit Committee Institute Survey 2016

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
- 09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

The company is required to announce any appointment or reappointment of a director to the AC<sup>182</sup>. It must state whether the Board considers the director to be independent. The company must also provide such additional disclosure as may be appropriate in the circumstances to enable its shareholders to assess the independence or otherwise of the appointed director. In the event of any retirement or resignation which renders the AC unable to meet the minimum number (not less than three) the company should endeavour to fill the vacancy within two months, but in any case not later than three months.

The Board should also disclose in the company's annual report the names of the members of the AC and the key terms of reference of the AC, explaining its role and the authority delegated to it by the Board. Members of the AC should be appropriately qualified to discharge their responsibilities.

According to the Guidebook for ACs, the AC should<sup>183</sup>:

- Have the ability to read and understand financial statements
- Possess the ability to understand and assess the general application of local or other generally accepted accounting principles
- Ask pertinent questions about the company's financial reporting process
- Effectively challenge management's assertions on financial information and management's responses when appropriate
- Understand internal controls and risk factors relevant to the company's operations, including those relating to information technology, treasury operations,

industry, financial derivatives, biological assets and mining concessions

- Have experience gained through executive responsibility for a sizeable business including having or having had responsibility for the finance function, such as being or having been a chief executive officer, chief financial officer or other senior officer with financial oversight responsibilities
- Possess education or professional qualifications relating substantially to accounting or finance.

The NC or the Board should carefully consider the length of term of each member. Rotation of AC members introduces new perspectives to AC processes, however, given the complex nature of the role, this has to be balanced with the need to have members who possess the necessary knowledge to discharge their responsibilities effectively.

### AC charter

For the AC to function effectively, the AC should define the scope of its oversight responsibilities and how these are to be discharged. The terms of reference for the AC should address the following:

- Roles and responsibilities of the AC, AC Chairman and its members
- Authority for the AC to seek independent professional advice at the company's expense
- Provision of direct access to anyone in the organisation to conduct any investigation to enable the AC to discharge its responsibilities
- Non-executive role of the AC which does not include making business or commercial decisions on behalf of management.

<sup>182</sup> Listing Rule 704(8) / Catalist Rule 704(7)

<sup>183</sup> Guidebook for ACs

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
- 09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Board Risk Committee ("BRC")

Although not mandatory, many large organisations have established a BRC in recent years. Many are often combined with the AC. If a BRC is established, its charter needs to be developed with reference to the intersection between its duties and those of other committees, particularly the AC.

BRCs generally have the following responsibilities:

- Review and approve the risk management policy for approval by the Board
- Oversee the implementation of the risk management framework
- Review management's plans for mitigation of the material risks faced by the company
- Monitor emerging risks and changes in the risk profile
- Promote awareness of a risk-based culture.

The ultimate responsibility for risk oversight rests with the full Board, regardless of whether or not a separate BRC is established. Further guidance is provided in the BRC Guidebook.

### Other common committees

A number of other committees often exist and are frequently chaired by directors of the Board to provide additional oversight on key risk areas, for example:

- WH&S committee – often used in high risk industries such as mining, petroleum and health, where staff are placed in complex production or service environments

- Information technology steering committee – generally in place where there is a significant reliance on information technology, such as call centres, emergency response services and technology service providers
- Research & development committee – often found where revenue generation is dependent on ongoing research activity, such as in the pharmaceutical and mining industries.

### Special Purpose Committee

Special purpose committees are usually established to consider a specific matter; they usually have limited terms. Nevertheless, the committee's charter or terms of reference should be approved by the full Board and the committee should follow the same operating principles as other Board committees.

Special purpose committees are often formed to deal with one-off events including:

- Takeovers, mergers, acquisitions or divestments
- Capital projects or system upgrades
- Reputation matters
- First-time adoption of significant laws, regulations, industry codes and organisational standards.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
- 09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices



## Case Study

In the case of Barings Securities (Singapore) Limited (BSS), Mr. Nick Leeson was employed as a general manager. He was not authorised to engage in trading activities. However, he took the necessary qualifications to trade, and soon became the de-facto leader of the back office, making it possible for him to approve unauthorised transactions and fabricate information to the main office of Barings Bank in U.K.



It was also found that the company did not heed warnings from internal audit reports which suggested Mr. Leeson was holding too many conflicting responsibilities. He manipulated the day trading books and created fictitious contracts in order to record profits in the reports that were sent to the head office in London. When the losses were discovered, Leeson was sentenced to six and a half years jail after incurring £827 million of losses which led to the bankruptcy of the bank.

This case highlights the importance of having a BRC that discharges its responsibilities of overseeing the implementation of a risk management framework and regularly review the various risks that are inherent and surrounding the business. With a committee on the Board to set out the guidelines and scope of the various risk inherent in their businesses, operations and investments, the company will be able to take up substantive measures to tackle these risks<sup>184</sup>.

<sup>184</sup> "Recent Cases on Corporate Governance in Singapore: The "Good", "Bad" and the "Ugly" by Tan Lay Hong (2009)

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
- ▶ 10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

# 10. Receiving Assurance

To assist the Board or Audit (and/or Risk) Committee to evaluate the adequacy and effectiveness of the company's risk management and internal control system.

## Questions that company Directors should ask

- |   |   |
|---|---|
| 1. Is the Board satisfied with management's assurances on the company's risk management and internal control systems?                             | 5. Is the Board, through the Audit Committee, satisfied that the internal audit function is operating effectively and efficiently?  |
| 2. Does the Board receive regular independent assurance on the adequacy and effectiveness of the business risk management framework and controls? | 6. Is the internal audit plan clearly linked to the up-to-date risk profile?  |
| 3. Has an assurance map been developed that provides a consolidated view on who provides assurance across the organisation's key processes?       | 7. Does the company have an adequate, effective and efficient integrated assurance framework – how do risk management activities integrate within the wider system of internal control? |
| 4. Does the external auditor test and challenge elements of the financial reporting, disclosure, risk and control environment?                    | 8. Does the governance and assurance framework add value to the organisation?   |

## Red flags

- |  |   |
|--|---|
| ▶ A compliance map does not exist to provide a gap analysis on assurance activities  | ▶ Internal audit projects are being cancelled or delayed by management                                |
| ▶ The Board does not review the risk profile and internal audit plan on a periodic basis   | ▶ Recommendations made by assurance providers are not being tracked and implemented                   |
| ▶ Uncertainty exists over the processes supporting management attestations   | ▶ The Audit Committee reports to the Board do not provide an overview of the internal audit work plan |
| ▶ The internal audit function appears to be under-resourced and not staffed with a team of experienced people who are kept abreast of developments and changes that may impact the internal audit work | ▶ There are significant accounting disagreements between management and the external auditor          |
|  | ▶ The external auditor is not present when the Board considers the annual financial statements        |



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
- ▶ 10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### What is assurance?

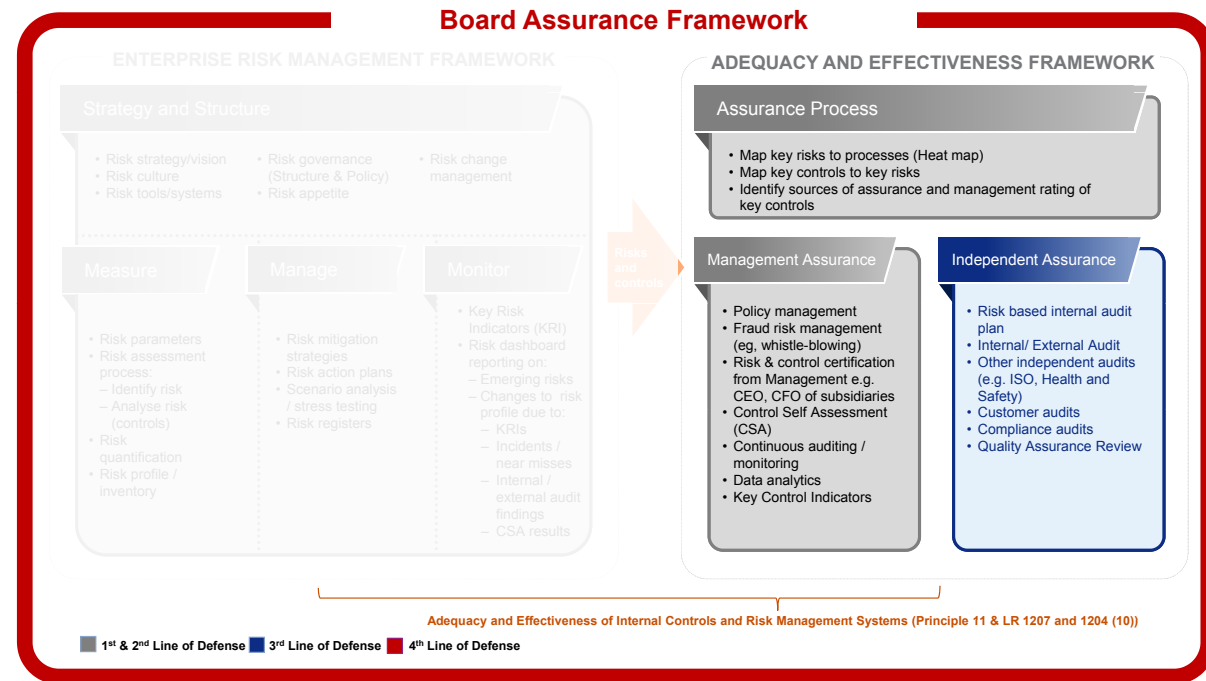
Assurance is an assessment process by which one can obtain a level of confidence over the matter at hand.

A robust governance framework will allow companies to be more resilient during economic downturns and respond better to changing legislation and regulations.

KPMG's Board Assurance Framework ("BAF") highlights a range of assurance activities that Boards could consider in reviewing the existing sources of assurance for their companies. This is to ensure the sources of assurance

provide accurate, complete and timely insights into the adequacy and effectiveness of the risk management and internal control framework.

Companies should adopt a balanced mechanism in obtaining assurance from management, its oversight functions and independent assurance providers as highlighted in KPMG's four lines of defence model below. The model can be used to structure roles, responsibilities and accountabilities for decision making across governance, risk management and assurance activities.

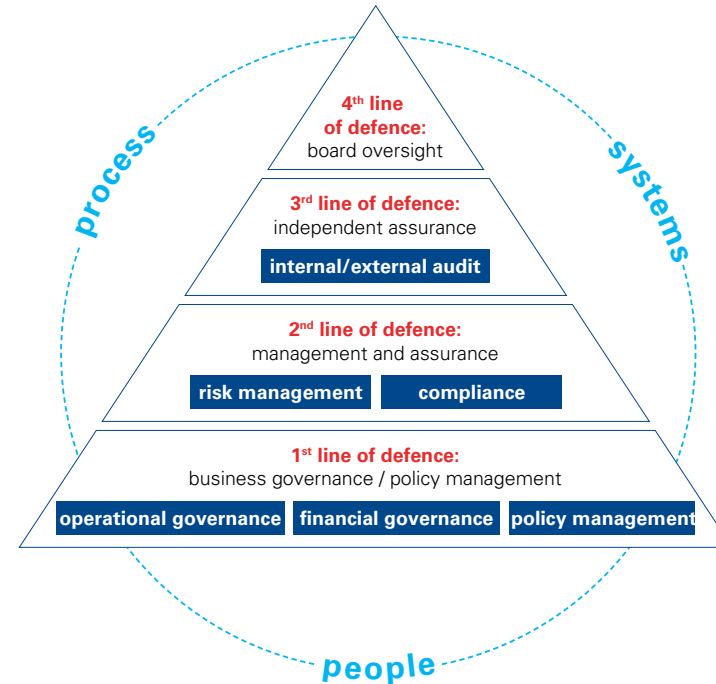


Source: KPMG's Board Assurance Framework

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
- 10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

## Overview – the four lines of defence in the control environment



As seen above, assurance can be received from several functions:

### 1. First line of defence: business governance / policy management

The Board may obtain some level of assurance on the risk and control environment of the company from management's attestation. The degree of assurance will depend on the robustness of the risk management framework. Line management should be adequately skilled to create risk definitions and make risk assessments. The risk profile should be periodically

reviewed and updated to reflect the changing business environment and emerging risks.

Continuous monitoring and regular risk reporting will allow the company to timely identify and address risks as they arise, thus conferring strategic advantage and opportunities over competitors.

The attestation can include:

- integrity of the financial reports
- adequacy and effectiveness of risk management and internal control systems covering financial, operational, compliance and information technology risk compliance with company policies and regulatory requirements.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
- 10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

The Board should review and comment in the annual report on the adequacy and effectiveness of the company's risk management and internal control systems, including financial, operational, compliance and information technology controls. In addition, the Board is required to disclose in the annual report whether it has received assurance from the CEO and CFO<sup>185</sup> indicating:

- (a) the financial records have been properly maintained and the financial statements give a true and fair view of the company's operations and finances; and
- (b) regarding the effectiveness of the company's risk management and internal control systems.

It is therefore paramount that the CEO and CFO establish mechanisms to enable them to provide assurance to the Board to identify significant risks and key controls to financial reporting and regarding adequacy and effectiveness of the risk management and internal control systems.

Management can use a control self-assessment ("CSA") programme to assess the control effectiveness and the business processes within the organisation. This tool is effective in identifying and assessing risks as well as designing the processes to address the risks, since employees' participation will raise their risk awareness and reinforce their responsibility for a robust control environment<sup>186</sup>. Management should present the results of the CSA, action plans and progress of implementation to the Audit Committee on a periodic basis.

Internal auditors or an external advisor can be engaged to assess the effectiveness of the CSA programme and this will also give an independent assessment to the Audit Committee with regards to management's attitude towards risk and control issues<sup>187</sup>.

## 2. Second line of defence: management and assurance

These are the groups which draft and implement policies and procedures and typically consist of people from Human Resources, Finance, Quality and Risk Management. They are responsible for providing direction and guidance in the implementation of policies and procedures. Their oversight of the business processes and risks would cover designing policies, setting direction, introducing leading practices, ensuring compliance and providing assurance oversight to the Board and Audit Committee.

Refer to Chapter 8 for more details on the oversight function of Risk Management.

## 3. Third line of defence: independence assurance

### Internal audit

The CG Code indicates that a company should establish an effective internal audit function that is adequately resourced and independent of the activities it audits<sup>188</sup>.

<sup>185</sup> CG Code Guideline 11.3

<sup>186</sup> Guidebook for ACs, page 77

<sup>187</sup> Guidebook for ACs, page 78

<sup>188</sup> CG Code Principle 13

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
- 10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

The internal auditor's role is pivotal in providing independent, objective assurance and consulting activities to the Board or the Audit Committee designed to improve the company's operations. It should be the major source of information to the Audit Committee on the performance of the entity. As such, it is imperative that the Audit Committee reviews and is satisfied with the effectiveness of the internal audit function<sup>189</sup> and that a strong relationship is forged between the two.

The Audit Committee's role relating to internal audit includes:

- Approving the overall charter of the IA function which includes role and scope of work, responsibility and accountability, objectivity and independence, operating principles, reporting, quality of service
- Reviewing and reporting to the Board annually, the adequacy and effectiveness of the company's internal controls, including financial, operational, compliance and information technology controls. This review can be carried out by an in-house internal audit department or by the outsourced consultant<sup>190</sup>
- Reviewing the adequacy and effectiveness of the company's internal audit function at least once a year. The AC should ensure that the function is adequately resourced and has appropriate standing within the company. The internal audit function should also be staffed with a team of experienced and qualified persons<sup>191</sup>

- When approving the internal audit budget and resource plan, the AC should ensure that the budget includes a detailed analysis of time and costs for each project. Where an external service provider is engaged, it is important that there is an engagement letter signed and internal audit plan developed to agree on the scope, deliverables and budget. The AC and the internal auditors also need to be kept abreast of the developments that may have an impact on the internal audit work, for example the changes in the CG Code, SGX LR and/or CA<sup>192</sup>
- Approving the risk-based IA plan. The plan needs to take into consideration the risk profile of the company so as to enable key risks to be prioritised and determine key areas to be audited. Emerging key risks should also be incorporated into the risk-based plan to ensure comprehensive coverage. The AC needs to be aware too that there may be areas or issues which require an independent third party reviewer to provide assurance or subject matter expertise
- Identifying the internal audit scope, procedures, coverage and timing of the audit and in particular any restrictions on the internal audit plan in advance of approving it to ensure that strategic business risks have been evaluated and auditable areas are prioritised in terms of timing and frequency, where necessary. The plan should also include a timetable setting out the commencement of the internal audit, completion of the audit reports and regular meetings between the Audit Committee and the internal auditor

189 CG Code Guideline 12.4 (c)

190 Guidebook for ACs, page 97

191 CG Code Guideline 13.2, 13.3 & 13.5

192 CG Code Guideline 12.8

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
- 10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

- Reviewing results of the internal audit activities or other matters that the internal auditor determines are necessary, including private meetings with the internal auditor without management's presence. It is essential that the Audit Committee has frequent communications with the internal auditor to review the reported findings and recommended improvements
- Making appropriate enquiries of management and the internal auditor to determine whether there are limitations in scope or budget which may impede the ability of the internal audit function to execute its responsibilities effectively.

Singapore's position in the global market, changes to corporate governance requirements and the dramatic changes in the business operating environment have increasingly brought about a need for the Board, through its Audit Committee, to seek broader assurances, beyond financial matters, in a range of areas, including WH&S, environment, security, information systems and human resources. These quality assurance needs have broadened the traditional internal audit function. The new-style internal audit model is aligned directly with corporate strategy and focuses on specific risks that impact on organisational success.

### External audit

The external auditor, having knowledge of the company's financial affairs, is also in a position to provide the Board assurance through the Audit Committee on the effectiveness of the entity's financial reporting and legislative compliance frameworks.

The primary objective of external audit is to add credibility to financial statements. The external auditor is to report to

the shareholders as to whether the financial statements of the company give a true and fair view of its financial position<sup>193</sup>.

Other functions that the external auditor carries out will also include assessing the internal control environment over financial reporting.

The AC typically has significant engagement with the external auditor throughout the year. Some of the key functions performed by the AC in assisting the Board in its oversight of the external auditor include:

- Recommending to the Board on the selection, appointment, rotation and removal (if necessary) of the external auditor. The AC should appoint a suitable audit firm that is registered with ACRA, registered with and/ or regulated by an independent audit oversight body acceptable by SGX or any other audit firm acceptable by SGX<sup>194</sup>. In addition, the date of the appointment and the audit partner's name must be disclosed in the company's annual report. The audit partner must be rotated out of the audit engagement after 5 years<sup>195</sup>
- Reviewing and (if appropriately authorised under the delegations framework) approving the terms of engagement and the reasonableness of audit fees prior to the commencement of the audit
- Reviewing the scope and results of the external audit. This can be done through reviewing the engagement letter to better understand the external auditor's roles and responsibilities, obtain a good understanding of the scope and approach that they will adopt in executing the audit plan

193 CA S201(3) & S207

194 SGX LR / Catalyst Rule 712(2)

195 SGX LR / Catalyst 713(1)



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
- ▶ 10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

- Meeting with the external auditor without management being present at least on an annual basis. It is important for the AC to communicate with the external auditor on matters relevant to the planning and completion of the audit. The AC should understand the overall audit strategy; materiality threshold and proposed resources (seniority and experience) to ascertain if they are consistent with the scope and external audit engagement. The AC should continuously challenge management and the external auditor about the:
  - Risks of material misstatement
  - Impact of changes in the business environment
  - Critical accounting principles
  - Subjective and judgemental accounting areas
  - Quality of financial reporting and disclosures
  - Changes to accounting standards.

The AC now meets and communicates with the external auditors more frequently, sometimes outside formal AC meetings. The intent is to forge a strong and candid working relationship with each other in order to gain additional insights into the company's risks, people, systems and processes supporting its financial reporting
- Reviewing independence and objectivity of the external auditor. Audit and non-audit fees should be disclosed in the company's annual report.

### *Other assurance providers*

Management may seek other assurance service providers depending on the nature of the company's business operations. This may include quality, clinical, training, safety and regulatory compliance audits.

The Board can put in place an overarching view on who provides assurance across the organisation's key risks. An assurance map can be used as a tool for the Board to outline the key business processes and risks. The assurance map should aim at providing the Board and AC confidence that:

- There is consistent, common and shared view on the level of appropriate assurance required for each risk
- There are no gaps in the level of expected assurance and no duplication of assurance
- Internal and external audit plans are aligned with the risk management framework
- There is accountability by management and/or external assurance providers
- Relevant parties are receiving assurance reports.

A formal escalation process should be established and the Board should be kept informed of all pertinent findings or issues arising from the assurance activities.

### *Evaluating control deficiencies with respect to the Risk Management and Internal Control systems*

A critical role of the Board is to manage risks to enable business objectives to be achieved. Understanding the key controls that are in place to manage risks and checking to determine their adequacy and effectiveness on an on-going basis is critical. Directors must ensure there is a structured process in place to evaluate, rectify and disclose control deficiencies (where required).

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
- 10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

Directors must satisfy themselves that there is sufficient evidence to comply with SGX LR 1207 (10) and Principle 11.3 of the Singapore CG Code. At a minimum Boards are required to provide an opinion as follows:

| Type of opinion<br>(in relation to SGX LR 1207(10) requirements) | Example disclosures  |
|--|--|
| Clean opinion  | The Board, with the concurrence of the Audit Committee, are of the opinion that the Group's internal controls, addressing financial, operational, compliance and information technology controls, and risk management systems were adequate and effective as at [date].  |
| Adverse opinion  | <p>The Board, with the concurrence of the Audit Committee, are of the opinion that the Group's internal controls, addressing financial, operational, compliance and information technology controls, and risk management systems were not adequate and effective as at [date].</p> <p>The following material deficiency(ies) were identified:</p> <p>1) <i>[Details of material deficiency to be provided]</i></p> <p>The following actions have been identified to address the material deficiencies:</p> <p>1) <i>[Details of actions to address material deficiencies to be provided]</i></p> |

The way in which Boards arrive at the opinion is varied. Illustrative guidance is provided in the Guidebook for ACs in particular Chapter 3 and Appendix C4.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
- ▶ 11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

# 11. Integrated Governance

The number of regulatory requirements for many geographies and industry segments means that companies are increasingly taking an integrated approach, rather than reacting to a specific regulation in isolation.

## Questions that company Directors should ask

- |   |  |
|---|--|
| 1. In which markets is the company listed? What regulations must you follow in those markets?   | 6. Is management kept abreast of changes in corporate governance standards?                                    |
| 2. Is there potential for the company to improve investor confidence by meeting stricter corporate governance standards of markets it is not listed in? | 7. Is management aware of the corporate governance expectations of some of the larger institutional investors? |
| 3. What are current shareholders expectations of corporate governance?  | 8. Is management aware of the diversity of corporate governance standards across different jurisdictions?      |
| 4. Who is in charge of making sure corporate governance standards are met?  |  |
| 5. Is the company in a position where it will be able to meet increasingly strict standards?  |  |

## Red flags

- |   |   |
|---|---|
| ▶ The company is dual-listed or multi-listed, but only follows the governance code of their primary listing           | ▶ Accountability for maintenance of the Board instruments is not clear                                      |
| ▶ No member of the Board is accountable for keeping up to date with corporate governance requirements and legislation | ▶ The company's annual report does not include all disclosures required by corporate governance legislation |
| ▶ Corporate governance rarely features on Board meeting agendas   | ▶ Directors are unfamiliar with best practice standards for corporate governance and risk management        |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
- ▶ 11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

Companies face an expensive and confusing regulatory landscape with changing laws and tougher enforcement. Given the number and mandates of regulators, it is no longer enough to adopt a reactive, episodic approach to compliance.

### Governance and regulation around the world

The first code of good governance was established in the US in the late 1970s, however, it was not until the UK's 1992 Cadbury Report and introduction of the Organisation for Economic Co-operation and Development (OECD) Principles that codes of good governance began to proliferate. Governance codes that followed included South Africa's King Report in 1994, the U.S. CalPERS Principles in 1998 and the SGX CG code in 2001. More recently, better practice recommendations have been

incorporated into the listing rules of stock exchanges around the world, including in Australia, Toronto, New York, and London. Multi-lateral organisations, such as the OECD, the International Monetary Fund (IMF), the World Bank and the International Corporate Governance Network are leading the charge for global standards of good governance.

This section references some key principles and governance codes for awareness from other jurisdictions.

### Organisation for Economic Cooperation and Development

The OECD Principles have been described as an international benchmark for corporate governance, a summary of which is included in this toolkit.

#### SUMMARY OF OECD PRINCIPLES 2015

##### Ensuring the basis for an effective corporate governance framework

The corporate governance framework should promote transparent and fair markets, and the efficient allocation of resources. It should be consistent with the rule of law and support effective supervision and enforcement.

##### The rights and equitable treatment of shareholders and key ownership functions

The corporate governance framework should protect and facilitate the exercise of shareholders' rights and ensure the equitable treatment of all shareholders, including minority and foreign shareholders. All shareholders should have the opportunity to obtain effective redress for violation of their rights.

##### Institutional investors, stock markets and other intermediaries

The corporate governance framework should provide sound incentives throughout the investment chain and provide for stock markets to function in a way that contributes to good corporate governance.

##### The role of stakeholders in corporate governance

The corporate governance framework should recognise the rights of stakeholders established by law or through mutual agreements and encourage active co-operation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises.

##### Disclosure and transparency

The corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, ownership, and governance of the company.

##### The responsibilities of the Board

The corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and the shareholders.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
- 11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Singapore

#### *The SGX Corporate Governance Code*

The SGX CG Code provides a set of corporate governance principles and guidelines for SGX listed entities, which are designed to promote investor confidence and to assist listed entities to meet stakeholder expectations. The SGX Listing Rules require listed entities to report against the Council's recommendations and, where they do not comply, to disclose that fact and the reasons why.

The SGX Corporate Governance Council revised the SGX Principles which were released on the 1 May 2012.

### Australia

#### *The ASX Corporate Governance Principles and Recommendations*

The ASX Corporate Governance Council's Corporate Governance Principles and Recommendations (ASX Principles) provide a set of corporate governance guidelines for ASX listed entities, which are designed to promote investor confidence and to assist listed entities to meet stakeholder expectations. The ASX Listing Rules require listed entities to report against the Council's recommendations and, where they do not conform, to disclose that fact and the reasons why.

The ASX Corporate Governance Council revised the ASX Principles which were released on 27 March 2014.

### United States (US)

#### *US Securities and Exchange Commission (SEC)*

The SEC regulates the US securities industry and enforces US federal securities laws. The SEC describes its mission as:

"... to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation..."

The laws and rules that govern the securities industry in the US derive from a simple and straightforward concept: all investors, whether large institutions or private individuals, should have access to certain basic facts about an investment prior to buying it, and so long as they hold it..." <http://www.sec.gov/about/whatwedo.shtml>

For more information about the SEC visit <http://www.sec.gov/>

#### *Sarbanes-Oxley Act*

The introduction of the Sarbanes Oxley Act (SOX) of 2002 in the US was a direct result of a number of major corporate collapses in late 2001. With the credibility of financial reporting falling sharply, the US congress responded with what George W. Bush described as, "The most far reaching reforms of American business practices since the time of Franklin Delano Roosevelt." As a result of the introduction of SOX compliance, management is now required to both assess and report on the design and effectiveness of internal controls over financial reporting. As a result, auditors evaluate and test a company's internal controls in a different light and in greater depth. The overall goal of SOX compliance is to strengthen internal controls over financial reporting, provide more reliable information to investors, and renew investor confidence in the US capital markets.

For more information on Sarbanes-Oxley visit <http://www.sec.gov/spotlight/sarbanes-oxley.htm>

#### *Dodd-Frank Wall Street Reform and Consumer Protection Act*

Following the global recession of the late 2000's the Dodd-Frank Act was introduced in the US to increase consumer protection, reduce or even eliminate 'too big to fail' corporate bailouts, and increase the transparency



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
- ▶ 11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

of credit rating agencies and exotic financial instruments, along with many other changes. The Act has been described as, "A rewrite of rules touching every corner of finance... the biggest expansion of government power over banking and markets since the Depression."

"Among other things, the SEC will require disclosure of any links, between executive compensation actually paid and the company's financial performance, taking into account any change in the value of the company's shares and dividends and any distributions." Chairman Sullivan and Cromwell, H.Rodgin Cohen.

Shareholders will also be asked to approve compensation of executive officers every 1, 2 or 3 years. For more information on the changes being implemented by the Dodd-Frank act see <http://www.sec.gov/spotlight/doddfrank.shtml>

### United Kingdom (UK)

#### *The UK Corporate Governance Code*

The Financial Reporting Council (FRC) is the UK's independent regulator responsible for promoting confidence in corporate reporting and governance. The FRC suggests that the UK's principles-based system of business regulation reduces the cost to global businesses of introducing procedures to comply with detailed regulations, many of which unnecessarily constrain business practice and innovation.

In that regard, the FRC has developed and reviews the Corporate Governance Code. The FRC notes that whilst it is expected that listed companies will apply the code's provision most of the time, it is recognised that departure from the provisions of the code may be justified in

particular circumstances. Every company must review each provision carefully and give a considered explanation if it departs from the code provisions. The code was last revised in September 2014.

### Asia

#### *People's Republic of China*

The China Securities Regulatory Commission and the State Economic and Trade Commission issued the Code of Corporate Governance for Listed Companies in China in 2002. The preface to the code states that it, '... is formulated to promote the establishment and improvement of a modern enterprise system by listed companies, to standardise the operation of listed companies and to bring forward the healthy development of the securities market of our country.' The code is applicable to all listed companies within the boundary of the People's Republic of China; and is used as a benchmark to assess whether a listed entity has a satisfactory governance structure.

#### *J-SOX*

'J-SOX' is an unofficial term for the Financial Instruments and Exchange Act that refers to Japanese requirements similar to the US Sarbanes-Oxley Act, Section 302 (management certification) and Section 404 (management evaluation and report on internal controls). J-SOX requires all public companies listed on stock exchanges in Japan to conduct management's assessment and reporting of internal control over financial reporting (ICFR) on a consolidated basis. As such, overseas subsidiaries and affiliates should also fall within the scope of such assessment and reporting.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
- 11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### South Korea

Code of Best Practices for Corporate Governance was first published in 1999 and made a significant contribution to enhancing governance of listed corporations. In 2002, there was a review of the code and in early 2003 a revised code was accepted. Whilst corporate governance in Korea has improved over the last decade, attributable largely to an increase in outside ownership and strengthened minority shareholder rights, many still have reservations about the quality of corporate governance in South Korea. The Korea Economic Institute attributes at least part of Korea's relatively low level of investment, poor price-to-earnings ratios and low production growth to a lack of high quality corporate governance.

For more information visit <http://www.keia.org/publication/progress-corporate-governance>

### India

The Securities and Exchange Board of India (SEBI) published a report on corporate governance in 2003 from the Narayan Murthy Committee evaluating the adequacy of existing corporate governance practices. In 2004 SEBI published a revised Clause 49 of the Listing Agreement relating to corporate governance, including changes to the composition of a Board's minimum numbers of independent directors, requirements for the Board to establish and maintain internal controls and take action where they are deficient, and mandates for the composition of an Audit Committee.

In addition, the Indian Companies Act was revised (effective from 1st October 2014) which includes a number of CG requirements.

For more information visit <http://www.sebi.gov.in/circulars/2004/cfdcir0104.pdf>

### Industry standards

To be able to effectively exercise their duties, directors must have an understanding of the company's business and the industry in which it operates, including a general awareness of any applicable industry standards or codes.

A high-level summary providing an example of these standards is included below.

### ISO 9000 and 9001

ISO 9000 is a set of quality management standards that provide a framework for processes and systems required for organisations to meet the needs of customers and other stakeholders. The standards are published by the International Organisation for Standardisation. ISO 9000 deals with the fundamentals of quality management systems, whilst ISO 9001 deals with the requirements that organisations wishing to meet the standards have to fulfil.

There is widespread use of these standards across many Singapore companies and industry segments.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
- 12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

# 12. Accountability to Shareholders

Listed public companies are jointly owned by an often relatively large number of separate shareholders, including both individual and institutional shareholders. Individual shareholders have different investment objectives which are based on varying degrees of financial and commercial understanding, literacy, competency and market intelligence.

## Questions that company Directors should ask

- |   |  |
|---|--|
| 1. Does the Board have a general understanding of the objectives of different investor groups and key individual investors? | 6. Does the Board have a process to ensure that all statutory reporting obligations are met in a timely manner?                          |
| 2. Does the Board receive regular briefings from the company's investor relations officer?                                  | 7. Is there a continuous disclosure policy approved by the Board and linked to the spokesperson policy?                                  |
| 3. Do the Chairman and directors play an active role in the investor relations program?                                     | 8. Does the Board regularly review the effectiveness of its business reporting and communications in assisting investor decision-making? |
| 4. Are mechanisms in place to capture market intelligence and investor feedback?  |  |
| 5. Is the Chairman always well prepared for questions from the floor at the AGM?  |  |

## Red flags

- |   |  |
|---|--|
| ► Major marketplace concern regarding executive remuneration incentives                                     | ► The SGX expresses concern regarding the timeliness of the organisation's market disclosures        |
| ► The AGM is a major public relations challenge   | ► The linkage between financial and nonfinancial reporting is not evident in external communications |
| ► The investor relations manager has no contact with the Board  | ► There is significant protest vote against the company's remuneration report                        |
| ► There is no strategy of how to handle private equity approaches   |  |
| ► Institutional investors publicly voice concerns regarding some of the organisation's governance practices |  |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
- ▶ 12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

The notion of accountability to shareholders is at the core of any corporate governance framework. Certainly shareholders are becoming more active in asserting their rights and many Boards are responding by trying to engage with their shareholders more effectively. Nevertheless Boards must balance the equitable treatment of shareholders and the protection of their rights against the need to create sustainable shareholder value.

### Protecting shareholders' rights

Companies should treat all shareholders fairly and equitably, and should recognise, protect and facilitate the exercise of shareholders' rights<sup>196</sup>.

A basic principle of corporate governance is that it should protect shareholder rights. These rights typically relate to, but are not limited to:

- Receiving dividends when declared or determined by the Board
- Approving changes to the company's Constitution or similar governing document
- Nominating and appointing directors
- Receiving continuous disclosure of material developments in the company's affairs<sup>197</sup>
- Calling a general meeting of shareholders, and/or proposing a resolution to be considered at a general meeting
- Voting at the AGM<sup>198</sup>
- Obtaining an independent valuation of their securities
- Inspecting the minute books for members' meetings
- Suing the corporation for wrongful acts

<sup>196</sup> CG Code Principle 14

<sup>197</sup> CG Code Guideline 14.1

<sup>198</sup> CG Code Guideline 14.2

- Allowing corporations which provide nominee or custodial services to appoint more than two proxies<sup>199</sup>.

### The Board's role

Some key Board roles in protecting shareholder rights:

- Maintaining a detailed understanding of shareholders' rights that are laid down in the CA, the SGX LR and other relevant legislation, together with the company's Constitution and Board policies
- Maintaining up-to-date knowledge of the company's beneficial shareholders
- Applying fiduciary duties and oversight processes to protect shareholder rights
- Ensuring shareholder communication is open and transparent
- Ensuring debate on contentious issues is embraced and prepared for
- Making the appropriate provisions in their Constitution to allow for absentia voting at general meetings of shareholders<sup>200</sup>
- Implementation of shareholder proposals approved by a majority of votes/proxies cast at a general meeting.

### Shareholder responsibilities

Shareholders have different investment objectives; some invest for short-term gain, some for long-term value and others invest for socially responsible reasons. Companies should actively engage their shareholders and put in place an investor relations policy to promote regular, effective and fair communication with shareholders<sup>201</sup>. Companies with an effective approach to investor relations will understand the objectives of different investor groups and

<sup>199</sup> CG Code Guideline 14.3

<sup>200</sup> CG Code Guideline 16.1

<sup>201</sup> CG Code Principle 15

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
- ▶ 12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

key individual investors. Communication and active engagement with shareholders generates feedback on investor concerns.

Certain shareholders, particularly some institutional shareholders, are becoming more assertive in protecting their own rights and are taking various measures to influence the companies in which they invest. These measures include:

- Communicating with the company openly and transparently
- Adopting a clear, comprehensive and pragmatic view of what constitutes good corporate governance
- Understanding and monitoring company performance and providing feedback to the company
- Teaming with like-minded shareholders to exert a collective influence
- Lobbying and targeted activism
- Adopting consistent positions, where appropriate, on particular issues and voting accordingly.

### The director's role in investor relations

The Board's role in formal investor relations continues to evolve. Many non-executive directors are now seeking to become more active in their companies' investor relations programs.

At a minimum, and in conjunction with the Board Chairman's traditional investor relations responsibilities, the Board should devise an effective investor relations policy to regularly convey pertinent information to shareholders<sup>202</sup> and approve any policies that control investor relations engagement risks. The Board should

<sup>202</sup> CG Code Guideline 15.1

also provide input into, and approve, the investor relations strategy as well as regularly monitoring investor relations activities. This strategy typically addresses an organisation's approach, performance targets and accountabilities for:

- Market intelligence and feedback mechanisms
- Shareholder and key stakeholder analysis and engagement planning
- Shareholder services (including share registry and transactional support)
- Investor targeting initiatives
- Shareholder and key stakeholder communications
- Media and public relations initiatives (including brand and reputation management).

Shareholders should have online access to comprehensive price, volume and trading data, as well as details of broker trading activity and company announcements on the SGX website<sup>203</sup>.

Regular dialogues with shareholders to gather feedback and address shareholders' concerns should also be established and maintained<sup>204</sup>. Such engagements with the shareholders should be stated in the company's annual report<sup>205</sup>.

Companies are also encouraged to have a policy on payment of dividends and should communicate it to shareholders<sup>206</sup>.

### Institutional shareholders' role in governance

Several sets of best practice principles have been published addressing the responsibilities of institutional

<sup>203</sup> CG Code Guideline 15.2

<sup>204</sup> CG Code Guideline 15.3

<sup>205</sup> CG Code Guideline 15.4

<sup>206</sup> CG Code Guideline 15.5



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
- ▶ 12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

investors. One such example includes the International Corporate Governance Network's (ICGN) Statement of Principles on Institutional Shareholder Responsibilities<sup>207</sup>, which sets out its view of the responsibilities of institutional shareholders in relation to their external role as shareholders and also in relation to internal governance. With respect to voting responsibilities, the ICGN suggests that institutional shareholders should:

- Disclose an annual summary of their voting records, together with their full voting records in important cases
- Seek to reach a clear decision, in favour or against, for each resolution on which they are expected to vote
- Disclose details of any outsourcing of ownership responsibilities (including the names of agents to whom they have outsourced, together with a description of the nature and extent of outsourcing and how it is regularly monitored).

### Convening the AGM

Directors are responsible for convening the company's AGM. If they fail to do so, any member of the company can apply to Court for an AGM to be held. To convene an AGM, a notice giving the details of the AGM must be served. Directors and co-directors must also prepare all the financial reports necessary for presentation during the AGM itself. The financial statements accompanied by the auditor's report must be sent to the members not less than 14 days before the AGM<sup>208</sup>.

### Notice for AGM

Notice of the AGM must be given in writing. It should be sent to all members (including the estate of a deceased member or the Official Assignee in charge of the affairs of a bankrupt member), the current auditor of the company (if any), and any other persons specified in the company's Constitution. The minimum period of notice is 14 days, though the Constitution may provide for a longer period of notice<sup>209</sup>. The notice period can, however, be shortened if all members of the company who are entitled to attend and vote at the AGM agree to it<sup>210</sup>.

Under certain circumstances, special notice may be required. For instance, a resolution to remove a director or auditor requires special notice. A special notice must be served to members at least 28 days before the date of the meeting<sup>211</sup>.

Notices may be served personally, by post, e-mail and other forms of electronic communication<sup>212</sup> or any other means permitted by the company's Constitution.

Other than the ordinary business of an AGM, the meeting should only deal with matters of which notice has been given. A resolution passed for anything not disclosed in the notice of meeting may not be legally valid if a voting member happens to be absent and therefore have no knowledge of the matter. Members also enjoy the right to propose resolutions themselves if they so wish, but must circulate them at their own expense<sup>213</sup>.

207 International Corporate Governance Network (ICGN), Statement of Principles on Institutional Shareholder Responsibilities, 2007 (Endorsed by the ICGN Board for member approval at the 2007 AGM).

208 CA Section 203(1)

209 CA Section 177(2)

210 CA Section 177(3)

211 CA Section 185

212 CA Section 387A & 387B

213 CA Section 183(1)

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
- ▶ 12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

Ordinary business of an AGM usually includes the following:

- Declaration of dividends
- Election of directors
- Appointment and fixing auditors' remuneration (if any)
- Consideration of the accounts, balance sheets and reports of directors and auditors
- Any business other than these will usually be classified as "special business".

### Shareholders' Resolutions

Shareholders exercise their decision making rights through voting on ordinary resolutions and special resolutions outlined below:

- Ordinary Resolution  
An ordinary resolution is a resolution that has been passed by a simple majority of over 50% of the votes cast by members entitled to vote, either in person or by proxy at the meeting.
- Special Resolution  
A special resolution is a resolution that fulfils the following conditions:
  1. Requires 75% or more of shareholder votes, either in person or by proxy at the meeting
  2. A written notice of the special resolution has been given to shareholders at least 21 days' in advance (for listed companies)<sup>214</sup>
  3. The notice must announce the intention to propose that the resolution involved be tabled as a special resolution.

### Lodgement of Resolutions

The Act requires that certain types of resolutions be lodged. Unless otherwise stated in the Act, every special resolution passed or every resolution which binds any class of shareholders must be lodged within 14 days after its passing<sup>215</sup>. Other than that, an ordinary resolution to allot shares is also required to be lodged<sup>216</sup>.

### Proxy

A shareholder with voting rights but who is unable to attend the AGM may appoint a proxy to attend and vote for him at the meeting. The proxy does not necessarily have to be a shareholder. A proxy appointed to attend and vote shall also have the same right as the shareholder to speak at the meeting<sup>217</sup>. Unless the Constitution otherwise provides, a proxy shall not be entitled to vote except on a poll and a member shall not be entitled to appoint more than two proxies to attend and vote at the same meeting<sup>218</sup>. Under the amendments to CA section 181, a new multiple proxies regime is introduced which allows corporations that provide custodial services to appoint custodial services to appoint more than two proxies.

### Poll voting

With effect from 1 August 2015, the new LR requires all resolutions at general meetings to be voted by poll. In addition, at least one scrutiner should be appointed for each general meeting to direct and supervise the count of the votes casted<sup>219</sup>. Voting by poll can accord shareholders with rights based on their respective shareholding.

<sup>215</sup> CA Section 186

<sup>216</sup> CA Section 161(5) & 186

<sup>217</sup> CA Section 181(1)

<sup>218</sup> CA Section 181(1A)

<sup>219</sup> SGX LR 730A

<sup>214</sup> CA Section 184(1)(b)

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
- ▶ 12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

Immediately after each general meeting and before the commencement of the pre-opening session on the market day following the general meeting, listed companies and trusts will have to announce whether the resolutions put to a general meeting of an issuer were passed. The announcement should include, amongst others, the breakdown of all valid votes cast at the general meeting, including information such as the total number of shares represented by votes for and against the relevant resolution and the total number of shares for a resolution<sup>220</sup>.

### Effective AGMs

Companies should encourage greater shareholder participation at general meetings of shareholders and allow shareholders the opportunity to communicate their views on various matters affecting the company<sup>221</sup>.

AGMs are governed by the CA (Section 174 to Section 176), the company's Constitution and in the case of meetings of listed companies, by the SGX LR. Public companies must hold an AGM of shareholders.

For many public companies the AGM is a major exercise in shareholder communication and investor relations. The AGM offers shareholders a unique opportunity to question the Board, express their views on company performance and suggest changes to company governance and operations.

As well as a forum for communication and discussion, the business of the AGM primarily considers the financial report and auditor's report, together with resolutions to approve the director's statement and report, and may include consideration of the appointment and remuneration of the auditor and the election and compensation of directors. Where the business of the meeting relates to the election (or re-election) of directors, shareholders will expect those directors to address them at the meeting.

As such, all directors should attend general meetings of shareholders. In particular, the Chairman of the Board and the respective Chairman of the AC, NC and RC should be present and available to address shareholders' queries at these meetings. The external auditors should also be present to address questions about the conduct of audit and the preparation and content of the auditors' report<sup>222</sup>.

220 SGX LR 704(16)  
221 CG Code Principle 16

222 CG Code Guideline 16.3

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
- ▶ 12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

The following are some key considerations for AGMs:

- A hostile AGM is rarely the result of spontaneous combustion. Boards in touch with shareholder concerns will anticipate and embrace debate on contentious issues
- Boards and management should spend time trying to anticipate specific shareholder questions and develop appropriate responses. Speakers should be identified in advance to respond on specific issues
- Difficult or contentious questions can sometimes be short-circuited by raising and answering them in the annual report, or in the formal Chairman's address to the meeting
- Shareholders can be invited to submit questions prior to the AGM
- Shareholders should be able to access a webcast of the meeting
- The Chairman should be thoroughly familiar with the AGM agenda and meeting procedures, and have developed an approach for dealing with difficult or hostile responses from the floor of the meeting
- The Chairman must allow a reasonable opportunity for members to ask questions about the management of the company.

Under certain circumstances, shareholders can also compel directors to call extraordinary general meetings of shareholders<sup>223</sup>, or seek to have resolutions added to the meeting agenda. Companies should avoid "bundling" resolutions for separate issues unless the resolutions are interdependent and linked so as to form one significant proposal<sup>224</sup>. All resolutions should be voted by poll and an announcement of the detailed results showing the

number of votes cast for and against each resolution should be made<sup>225</sup>.

Minutes of the general meeting should be prepared with substantial and relevant comments or queries from shareholders relating to the agenda of the meeting, and response from the Board and management included, and to make these minutes available to shareholders upon their request<sup>226</sup>.

There have been increased efforts by Boards of directors to engage shareholders in less contentious, more cooperative interaction and communication. Shareholders are also encouraged to consider how they, in turn, might foster more constructive relationships with corporate Boards, through consideration of the appropriate limits of shareholder power<sup>227</sup>.

### Statutory reporting and SGX Continuing Listing Obligations

Shareholder and investor communication starts with statutory reporting. For SGX listed companies in Singapore, statutory reporting is based on:

- The CA
- Singapore Financial Reporting Standards
- Interpretations of Financial Reporting Standards issued by the Accounting Standards Council
- SGX LR
- Singapore Code of Corporate Governance (non-statutory)

<sup>225</sup> CG Code Guideline 16.5

<sup>226</sup> CG Code Guideline 16.4

<sup>227</sup> Rethinking Board and Shareholder Engagement in 2008, By Weil, Gotshal & Manges LLP

<sup>223</sup> CA Section 176

<sup>224</sup> CG Code Guideline 16.2

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
- ▶ 12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

Non-statutory reporting is based on:

- Singapore Code of Corporate Governance
- Sustainability Reporting

The key elements of the statutory and non-statutory reporting portfolio for listed companies include:

- Quarterly, half-yearly and full year reporting
- An annual audited financial report and (directors' statement)
- Corporate Governance Statement<sup>228</sup>
- Sustainability Reporting
- Notices for AGM
- Additional disclosure requirements.

Whilst it is common practice for the Board to allocate the oversight of statutory reporting to its Audit Committee, or equivalent, it is unable to abrogate its ultimate responsibility for the accurate and thorough preparation and timely release of statutory reports. Consequently, all directors need to understand not only the content of the reports, but what reports are required and by which authorities.

Boards need to exercise appropriate due diligence in matters of financial disclosure. False or misleading statements could leave directors personally liable under the CA.

Boards should also insist that effective systems are in place to ensure that all formal shareholder and investor communications (including financial reports):

- Result from a designated approvals process
- Include all the information required by the relevant laws and standards
- Adhere to statutory timing requirements

- Follow the format prescribed by the relevant laws and standards
- Produce information that is accurate and not misleading.

Some companies may also have reporting requirements to overseas regulators. For example, the US SEC require foreign registrants to file a number of reports and documents, including the comprehensive Form 20-F annual report of a Foreign Private Issuer.

Unless members specifically elect to receive a hard or electronic copy of the annual financial report, companies or schemes can provide the annual financial report (or concise report) to its members by making it readily accessible on a website and by directly notifying members in writing that it has done so.

### Statutory reporting content

Detailed guidance on the contents of the financial statements and notes to the financial statements can be obtained from KPMG's Singapore Illustrative Financial Statements and KPMG's Insights into IFRS series of publications.

### Annual report

Depending on the entity's structure and jurisdiction, there are varying reporting requirements that must be adhered to. Directors should be aware of the reporting requirements and obligations applicable to jurisdictions in which they operate. For example, a publicly listed entity in Singapore is required to adhere to the statutory reporting requirements and any other legislation applicable to the



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
- ▶ 12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

entity type. For this reason, the contents of an annual report should include, at a minimum:

- Full set of financial statements, as defined by CA and Singapore Financial Reporting Standards 1, including the statement of financial position, statement of comprehensive income, statement of cash flows and statement of changes in equity and explanatory notes
- Directors' statement
- Auditor's report
- Corporate governance statement.

Increasingly, however, companies are choosing to include additional material in their annual reports. Emerging areas of optional reporting include sustainability which is being used to not only satisfy stakeholder demands for extra information, but as a proactive step in the stakeholder management process.

### Directors' statement

The directors' statement should include a solvency statement and mention of whether the financial statements and notes have been prepared in accordance with the Singapore Financial Reporting Standards and the CA.<sup>229</sup>

When forming its opinion on the solvency of the company for the directors' statement, a Board is obliged to consider the debts of the company as at the date of the statement, not merely those debts included in the balance sheet as at balance date. Directors should obtain all relevant information so that they can form an opinion about the company's solvency.

Those dissenting from the resolution should be identified and their reasons stated. A Board may qualify

its statement. This could occur, for example, if there is a material uncertainty about the company's ability to renegotiate loans for repayment. A qualified statement will not of itself limit the liability of directors, nor will it operate as a substitute for the proper discharge of their duties.

### Auditor's report

An auditor must report to members on whether the auditor is of the opinion that the financial report is in accordance with the CA, including compliance with the Singapore Financial Reporting Standards and International Financial Reporting Standards, and that the financial report provides a true and fair view of the financial position and performance for the financial year.

The auditor's report must also describe any defect or irregularity in the financial report and any deficiency, failure or shortcoming relating to:

- Obtaining all information, explanations and assistance necessary for the conduct of the audit
- Keeping sufficient financial records to enable a financial report to be prepared and audited
- Keeping other records and registers required by law<sup>230</sup>.

### Other disclosures in the annual report

The SGX requires listed companies to provide a statement disclosing the extent to which it has followed the CG Code for each reporting period<sup>231</sup>. Although the recommendations are not prescriptive, a company that does not follow a recommendation must explain so on an 'if not, why not basis'. This is generally done in a separate corporate governance statement.

<sup>229</sup> Twelfth schedule of the Companies Act, Contents of Directors' Statement Section 1 (a) and (b).

<sup>230</sup> CA Section 207(2)(b)

<sup>231</sup> SGX LR 710

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
- ▶ 12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

In addition to statutory disclosures, many companies include additional information in their annual reports, such as overviews of business strategies and key drivers, and non-financial performance measures, and they convey these areas using snapshots, charts, artwork and photographs.

They might also, for example, use the annual report to indicate their environmental achievements and compliance record, and to report on various communities, social and corporate citizenship initiatives.

In approving the content and format of annual reports, Boards should keep in mind the following points:

- As far as directors are concerned, the annual financial reporting parts of annual reports are legal documents – compliance with the legal requirements remains a key consideration for any Board
- Awareness of annual reporting best practice for the nature and extent of disclosure, and for the presentation of information
- Good reports usually incorporate a straightforward, logical and accurate account of the company's performance, together with a simple explanation of how the company intends to tackle the opportunities and problems confronting it
- Whether it is more suitable to make the annual report readily available online or to distribute hard copies to shareholders.

### Summary version of annual reports

The CA<sup>232</sup> now permits all companies to distribute to shareholders summary financial statements of their annual reports. The summary report must be prepared

in accordance with the Singapore Financial Reporting Standards, and must contain some discussion and analysis of the position and results of the company to accompany the summary financial statements. The summary report must be audited and a full report must be provided to members if they request it.

### Quarterly and half yearly reports

A disclosing entity must prepare a financial report for each quarter (if required) and half-year. There is no requirement for these reports to be audited or reviewed. More detailed guidance on quarterly, half-year and full year announcements can be obtained from SGX LR Appendix 7.2 Financial Statements and Dividend Announcement.

### Audit Committee

Boards should ensure that the internal governance systems include adequate involvement of the external auditor, internal audit and the Audit Committee. The terms of reference of the Audit Committee should include a role in the review of significant financial disclosures before sign-off by the full Board.

The Audit Committee typically focuses on a limited range of key issues for statutory reporting purposes. It should review:

- Any significant accounting and reporting issues, including professional and regulatory announcements, and understand their effect on the company's financial statements
- All quarterly, half-yearly and full year results announcements and annual financial statements of the company, and any other periodic disclosures, that require approval of the Board (the process typically culminates in a detailed page-by-page review by the Audit Committee of these reports with the external auditor and management present)

232 CA Section 203A(1)

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
- ▶ 12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

- The assurance provided by the CEO and CFO<sup>233</sup>
- The processes, policies and procedures for compliance with the company's continuous disclosure obligations
- All related party transactions for potential conflicts of interest, providing approvals on an ongoing basis.

### Investor decision-making

If companies are to maximise returns to their shareholders, they must not only create value, but be seen to have created value and provide prospects for value creation in the future. This is essentially a matter of communicating with shareholders, potential shareholders and third parties in a position to influence investors' share buying, retention and selling decisions.

Regular and effective reporting and communications between the company and these parties influences the decision-making of shareholders and potential investors.

It is, however, widely acknowledged that traditional information flows (e.g. general purpose statutory financial reporting) and engagement practices (e.g. AGMs) do not typically address the broad range of issues of concern to individuals and entities seeking to make timely, accurate and precise decisions on their investments, or potential investments, in the company. Therefore, companies need to address the limitations of traditional reporting to fulfil their intended purpose and seek ways to better inform investors.

A new model of business reporting and communication that creates reports based on what the company wants to communicate – and on what investors want and need to know – can ensure that shareholders will make the right decisions, at the right time, about the things that matter to the company – particularly investment opportunities.

Reporting and communication strategies should be directed to balancing the performance/ reward equation and aligning business rewards – capital, licences to operate and reputation – with company performance.

Integrated reporting of this kind articulates the:

- Business strategy
- Performance in executing the strategy
- Insights about the drivers of and risks threatening the successful execution of the strategy
- Outlook for future performance if the strategy is well executed.

This model implies specific reporting on performance drivers, such as infrastructure, people, business processes, strategic management, risk management and governance performance, and the dynamic interplay between all of these factors.

Through integrated reporting, shareholders can gain an appreciation of the strength of the business model in terms of its:

- Velocity (speed of business processes)
- Versatility (flexibility and agility in the face of changing external forces and market conditions)
- Vulnerability (to shocks from business risks)
- Volatility (consistency of business processes in the face of change).

Reporting and communication must be underpinned by rigorous business modelling and measurement methodologies. The business modelling methodology is required to support clear and precise reporting of the business strategy and model in a form that can be easily understood and acted upon by key shareholders and investors.

233 CG Code Guideline 11.3

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### ► 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

Business reporting and communication methodologies and tools help organisations decide what to report, in what format, to whom and when. Among other things, the process requires a filtering mechanism centred on balancing the measurement power of particular key performance indicators, including those relating to risk management (an information supply perspective), and how and when key shareholders and investors can and should build strategy, performance insights and outlook into their decision-making models (an information demand perspective).

The reporting and communications strategy needs to detail how and when the organisation can enhance investment decision-making models and influence investment decision-making behaviours.

### The Board's role in business reporting

Business reporting should accurately reflect and communicate the real corporate picture. Boards are in a unique position to step back from the day-to-day perspective of management and view the organisation from all perspectives. Boards should be able to assist in improving the quality of reporting by identifying any major gaps between what is being reported to shareholders and investors by management and what should be reported, whilst having regard to stakeholder needs, concerns, influences and decision-making behaviour.

Thus Boards are actively seeking a new reporting framework to help them decide on what to report, when, to whom, in what format and why. However, there are many impediments to change including:

- The risk of litigation if forward-looking statements are not met

- The release of competitively sensitive information or information that may be subject to rapid change or volatility
- A lack of willingness on the part of competitors and industry participants to be more forthcoming with voluntary disclosures
- No agreed industry reporting standards
- Concern that capital markets will not cope with/ synthesise the extra information
- Markets being only interested in short-term performance.

There are a number of ways to improve business reporting, including:

- Encouraging more direct involvement by the Board
- Aligning internal reporting with external reporting (statutory reporting, results announcements and investor presentations, corporate social responsibility reporting, other more frequent reporting such as pro-forma/non-GAAP earnings guidance, production reports or balanced scorecards looking at the performance of non-financial KPIs)
- Improving consistency and clarity in the company's message (strategic goals/objectives) and the linkages between financial and non-financial reporting
- Streamlining reporting and creating a balanced portfolio of reports
- Educating shareholders on the implications and value of reporting changes
- Using technology for reporting automation and diffusion (e.g. XBRL, web-based and real-time reporting, enterprise and data modelling).

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
- 13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

# 13. Stakeholder Engagement

Evolving community expectations of the corporate sector are resulting in effective stakeholder engagement emerging as a critical success factor for the long-term sustainability of operations.

## Questions that company Directors should ask

- |   |  |
|---|--|
| 1. Is the Board comfortable that it knows who its key stakeholders are?   | 6. Do relationship effectiveness measures exist for key stakeholders?  |
| 2. Have stakeholders with the ability to affect strategic and business objectives been engaged effectively?                     | 7. Is the Board seeking and maintaining relationships with its key stakeholders at the leadership level?                   |
| 3. Have the risks of not engaging key stakeholders (financial and reputational) been considered and, if applicable, quantified? | 8. Has the company considered making a public disclosure about stakeholder management and corporate social responsibility? |
| 4. Is stakeholder engagement embedded into the company's vision, mission and strategy statements?                               | 9. Is effective stakeholder management used as a strategic, preventive mechanism, rather than a responsive tool?           |
| 5. Does the company have a stakeholder engagement framework aligned with best practice?   |  |

## Red flags

- |  |  |
|--|--|
| ► The company maintains no stakeholder mapping, tiering or profiling information | ► The risk of not engaging stakeholders is not discussed or is often dismissed quickly by some Board members |
| ► Stakeholders are defined narrowly as clients and customers                     | ► Dialogue with stakeholders mostly occurs in the event of disputes and negative media coverage              |
| ► In most decisions, stakeholders are not considered or consulted                | ► Online coverage of the company is mostly negative  |



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
- ▶ 13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Stakeholder engagement

The Board's role is to ensure that obligations to shareholders and other stakeholders are understood and met<sup>234</sup>.

Stakeholder engagement is the process of identifying and involving the key groups of people and organisations who are affected by, or have the capacity to influence, the company's activities and operations.

Ordinarily, a Board's direct involvement with its key stakeholder groups may be limited to the Chairman or the respective chairmen of the Audit Committee or the Environmental Committee, where the latter exists. In extraordinary circumstances (e.g. crisis mode) the wider Board may become involved in engagement activities and communication.

However, management is now turning to directors to tap into expertise and relationships to facilitate engagement, advocacy and lobbying with key stakeholders. Directors who possess 'change agent' competencies can be influential in championing particular courses of action. Although there is no legal standard or requirement for formal stakeholder engagement, most directors now consider that their Boards could, and should, be much more effective in their understanding and oversight of key stakeholder engagement strategies.

### Why focus on engaging stakeholders

Companies exist within an environment where there is increasing scrutiny over the sustainability and integrity of their operations. In the same way as companies perceived as acting in a detrimental fashion can suffer loss, companies that collaborate with and mobilise their

stakeholder base are able to present a positive public image and reap the rewards of the reputational and financial benefits that follow.

Other than reputational and public perception implications, for some companies certain revenue (i.e. government contracts) can be dependent on the fulfilment of sustainability, community relations and other stakeholder engagement criteria. For such arrangements, effective stakeholder engagement processes are essential in providing companies with the ability to compete with their industry rivals.

### Establishing an effective shareholder engagement framework

In establishing a stakeholder management function, companies are increasingly formalising the arrangements and processes, including developing stakeholder engagement plans.

Common themes of sound stakeholder engagement frameworks include:

- Stakeholder maps and tiering
- Responsibilities for developing relationships with agreed accountabilities (Board and management)
- Defined methods for gathering information on stakeholders (i.e. surveys, research, etc.)
- Methods and accountabilities for monitoring stakeholder concerns, influences and sensitivities
- Established positions on relevant public or industry-specific policies
- A variety of methods of communication, including forums, meetings, and site visits, etc.

234 CG Code Guideline 1.1(e)

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
- ▶ 13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

The *AA1000 Stakeholder Engagement Standard* (AA1000SES) provides an internationally recognised framework to help organisations ensure stakeholder engagement processes are purpose driven, robust and deliver results, and form a basis for designing and implementing effective stakeholder engagement in a credible way<sup>235</sup>.

### Stakeholder engagement beyond the customer base

Stakeholders in companies can include:

- Regulators and government
- Employees and unions
- Customers and suppliers
- Local communities and environmental advocacy groups
- Lobby groups and representational bodies.

The concerns of these stakeholders are not just financial; they span the so-called 'triple bottom line' of financial, social and environmental objectives.

### Stakeholder engagement at a Board level

Companies with effective stakeholder engagement possess a common theme of a strong 'tone at the top'. Boards are responsible for setting the general policies and direction of the organisation. They shape the organisation's framework for accountability and they should lead by example in fostering an outward looking approach by collaborating with stakeholders, ensuring mutual benefit from business dealings and acting with integrity.

<sup>235</sup> For further information please refer to AA1000 Stakeholder Engagement Standard <http://www.accountability.org/images/content/3/6/362/AA1000SES%202010%20PRINT.pdf>

At a Board level, stakeholder engagement should be defined as a core organisational value. Directors should identify the key risks associated with evolving societal expectations and set expectations with their executive management group around effectively engaging the stakeholder base. Further, the Board should also consider their own interface with their stakeholders, being the integration of stakeholder issues into the AGM, public reporting and invitations for senior stakeholders to periodically address Board meetings.

### Reputational advantages of effective stakeholder management

***"It takes 20 years to build a reputation and 5 minutes to ruin it."***

Warren Buffet

A good corporate reputation is a prized asset that is earned over time. It can be a source of competitive advantage, influencing the level of engagement with the company by employees, customers, suppliers and other stakeholders. By way of contrast, failure to manage reputation can have a deleterious and prolonged effect on a business. Reputation damage affects directors' personal reputations, employee morale, investor confidence and company performance. Reputation risk has been identified as one of the most important risks a company faces. Loss of reputation, however, is usually the result of poor risk management processes across all risk areas, including compliance, finance, environmental considerations and operations. A robust and systematic enterprise-wide risk management strategy is essential to maintain a company's reputation.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
- 13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

In turn, a company's reputation is directly linked to the Board's role in both strategy and risk. The Board's starting point in developing a positive corporate reputation is the right 'tone at the top', fostering appropriate organisational values that drive organisational culture. A reputation management system, underpinned by straightforward and open communications, protects this intangible, but vital asset. Some companies are going further, defining and measuring their reputation and benchmarking it against other participants in the market.

Despite the best risk mitigation program, when things go wrong, a period of reputational volatility can ensue. Reputation is affected by the way an accident/incident is managed and/or the company's ability to react to and handle such a crisis. The company needs to prepare itself for potential such catastrophe. The media is a critical influencer of public opinion, especially in a crisis.

### The emergence of 'tax morality'

Managing tax risk is becoming an increasingly important challenge. Companies are realising that tax requires strategic direction at Board level. An effective response to the changing world of tax can bring significant financial benefits through the optimisation of the organisation's effective tax rate.

Fundamentally, attitudes and approaches to tax are changing. As globalisation continues to change corporate structures and the tax arrangements of global companies are increasingly entering the world of corporate social responsibility. Now, tax and the issue of paying 'your fair share' is one of the most prominent areas being scrutinised by governments, the general public and, to a great extent, the media. Just like corporate responsibility and environmental issues, brand damage can occur if there is a perception that a company's tax affairs are perceived as overly aggressive or 'unfair'.

#### RECENT EXAMPLE – How Starbucks avoids UK taxes (Oct 2012)

For the past three years, Starbucks reported no profit, and paid no income tax, on sales of 1.2 billion pounds in the UK. However, transcripts of investor and analyst calls show that Starbucks officials regularly comment that the UK business is "profitable" and cited it as an example to follow for operations in the United States. Three means in which Starbucks evaded taxes were identified. Firstly, royalties on intellectual property, by housing intellectual property units in tax havens, and charging their subsidiaries fat royalties for using it. For example, fees from Starbucks' European units are paid to Amsterdam-based Starbucks Coffee EMEA BV, described as its European headquarters. The CFO, Troy Alstead further claimed that revenue was burnt up on staff costs and rent while the HQ only had 97 employees. Secondly, it is the requirement to allocate some funds generated in the UK to other subsidiaries in its supply chain, also known largely as "transfer pricing". Thirdly, was the use of inter-company loans done by shifting profits to low-tax jurisdictions? This allows the borrower to set any interest paid against taxable income while the creditor can be based in a place that does not tax interest.

Source: Special Report - How Starbucks avoids UK taxes

<http://uk.reuters.com/article/uk-britain-starbucks-tax-idUKBRE89E0EW20121015>

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
- ▶ 14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

# 14. Private Equity

Private equity (PE) deals are now being transacted with heightened corporate governance expectations. Directors operating in this environment will need to understand their governance responsibilities, issues and priorities.

## Questions that company Directors should ask

- |  |  |
|--|--|
| 1. Do we possess the protocols for managing conflicts of interest with participating directors and/or management?        | 6. Should a broader sale process be initiated to maximise shareholder value?   |
| 2. Do we understand the potential personal financial upside to management from a PE deal?                                | 7. Is the Board clear on its requirements regarding when and what to disclose to the markets?  |
| 3. Are protocols in place to secure independent review of any approach?  | 8. Does the Board have a 'defence protocol' for a potential approach by a prospective bidder that enhances the company's responsiveness and mitigates potential risks? |
| 4. Do we need to set up an independent sub-committee to lead decision-making and process-manage a potential transaction? | 9. Does the Board discuss the approach or the proposed transaction in closed sessions without participating directors and management?                                  |
| 5. Does the Board understand the position of key shareholders?   | 10. What will the impact of the PE approach have on the Board's normal agenda?   |

## Red flags

- |  |   |
|--|---|
| ▶ The Board has in the past been caught unaware by PE bids   | ▶ Directors' messages are inconsistent or unclear regarding their position on PE bids |
| ▶ No strategy has been developed for dealing with PE bids and it is rarely discussed at Board meetings | ▶ Independent advisers are usually not engaged to examine PE submissions              |
| ▶ Continuous disclosure issues have been raised against the company over past PE bids                  |   |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
- ▶ 14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### What is private equity?

The term private equity (PE) covers a broad range of activities related to investing in unlisted companies. It may include taking listed companies private. It represents an alternative model to that of the dispersed ownership of a publicly listed entity.

### Pre-private equity considerations for Boards

Boards need to be on the front foot when PE does come knocking. A plan of action developed beforehand regarding how to respond to a bid, be it from PE or anyone else, is a good idea.

A Board cannot leave the initial response to a PE approach to management, which is very likely to possess a conflict through its involvement in the transaction via a management buyout.

The Board's fiduciary duty is to continue to act in the best interests of shareholders. Directors should consider:

- Understanding whether the PE approach is a 'sounding out' conversation or an immediate precursor to a bid
- Obtaining market perceptions reports
- Procuring up-to-date valuations (can set the tone for subsequent negotiations and discussions)
- Arranging a panel of selected advisers (speaking with them in closed sessions without management)
- Ensuring policies are appropriate and clear (e.g. conflict of interests)
- Setting ground-rules (roles and responsibilities) for the Board, Chairman, Board committee and individual director involvement
- Understanding the shareholder base (current and future) and the role a PE investor might have as a

potential source of funding for future growth and expansion strategies

- Establishing a due diligence process, particularly around the degree of access, if any, that may be granted to this or any other bidders, and areas of possible synergies from merging with potential bidders (which may be part of a defence/price maximisation strategy)
- Providing institutional investors with enough information for them to do their own valuations.

Despite the focus and commitment in dealing with a PE approach, it will be business as usual at the front line. The Board also needs to consider the impact of an approach on its normal agenda. To assist with this, and to isolate directors who may have a conflict of interest, an ad hoc Board committee can take control of the company's response to a PE offer.

This Board committee should:

- Comprise independent directors who are free of conflicts
- Have access to its own advisers who are also free of conflicts
- Possess appropriate authority
- Pay careful attention to the documentation presented and produced (and if necessary, have the authority to obtain an independent fairness opinion/valuation)
- Tightly monitor continuous disclosure and any transparency issues with price sensitive information during the transaction (including decisions on when to go public and the control and provision of confidential information by independent directors to the Board and management)
- Continuously monitor the market for other possible opportunities.



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
- ▶ 14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

The committee needs to be open-minded, willing to take advice and consider all options and alternative strategies (defence strategies, further independent valuation, auction strategies and overcoming impasses).

The existence of the committee does not, however, relieve other directors of their obligations under the CA and SGX LR during PE activity. The key objective is to provide good counsel to shareholders on the PE proposal.

### PEC Board considerations

In principle, Private Equity Committee (PEC) Boards should observe many of the same governance practices adhered to by publicly listed companies. The OECD has rejected calls for different and separate corporate governance guidelines for PECs, whereas some venture capital associations have issued broad governance guidelines for PECs to observe<sup>236</sup>.

The PEC Board is typically structured in the best interests of the investee company. The composition of the PEC Board will inevitably change with greater representation from the PE investor. Good practice includes maintaining an independent Chairman and ensuring that a majority of directors are independent.

A PEC Board consequently tends to be smaller due to the high cost of appointing independent non-executive directors. However, Board appointees should continue to be individuals of appropriate competencies, skill and experience who can provide value and insight to the PEC. The relationship between the Board and management should be clear and supported by the appropriate documentation of roles and responsibilities, with effective conflict of interest policies. In some cases, the Board develops and monitors a 'management agreement' between the investors, the Board and management to assist this cause. The Board's charter depends on what the PE owners expect. This may also be dependent on what the lender(s) demand. Some roles and responsibilities may also change (e.g. Audit Committee, etc.).

As many PECs eventually re-emerge as publicly listed entities, PEC Boards will be better served if their governance frameworks allow a seamless transition to public trading.

<sup>236</sup> European Private Equity and Venture Capital Association (EVCA), EVCA Handbook, Profession Standards for the Private Equity and Venture Capital Industry (Edition November 2012) [http://www.evca.eu/uploadedFiles/Home/Toolbox/Industry\\_Standards/EVCA\\_Handbook\\_November\\_2012.pdf](http://www.evca.eu/uploadedFiles/Home/Toolbox/Industry_Standards/EVCA_Handbook_November_2012.pdf).

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
- ▶ 15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

# 15. Establishing a New Board

Establishing a new Board is a challenging responsibility. Implementing the corporate governance framework, appointing the CEO, endorsing Board instruments, embedding the right culture and setting the strategic direction are the crucial first steps in setting up an effective Board.

## Questions that company Directors should ask

- |  |   |
|--|---|
| 1. Do we have a structured plan, with timeframes and accountabilities on how to establish the Board? | 4. Are we aligning our frameworks, policies and appointments with our strategy? |
| 2. Do we have the support, resourcing and experience we need to deliver?                             | 5. Is the Board defining its 'risk appetite'?                                   |
| 3. Are there clear priorities on what needs to be looked into first?                                 | 6. Do we have access to better practice frameworks and instruments?             |

## Red flags

- |   |   |
|---|---|
| ▶ There is no consensus on the initial priorities   | ▶ No time has been planned for discussing alignment with 'risk appetite' and strategy   |
| ▶ There is limited understanding on what is required in the establishment phase                       | ▶ There is no clear establishment and documentation of accountabilities and delegations |
| ▶ The Board comprises mainly inexperienced directors  | ▶ No Board instruments have been presented for review and approval                      |
| ▶ No advice is being sought from experts or directors who have experience in establishing a new Board |   |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
- ▶ 15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### The first 100 days framework

Directors appointed to newly formed Boards are required to oversee the challenging task of establishing a functioning boardroom and effective corporate governance structure.

The first 100 days framework provides a high-level roadmap of the key activities and deliverables required to establish an effective Board within a target timeframe of 100 days.

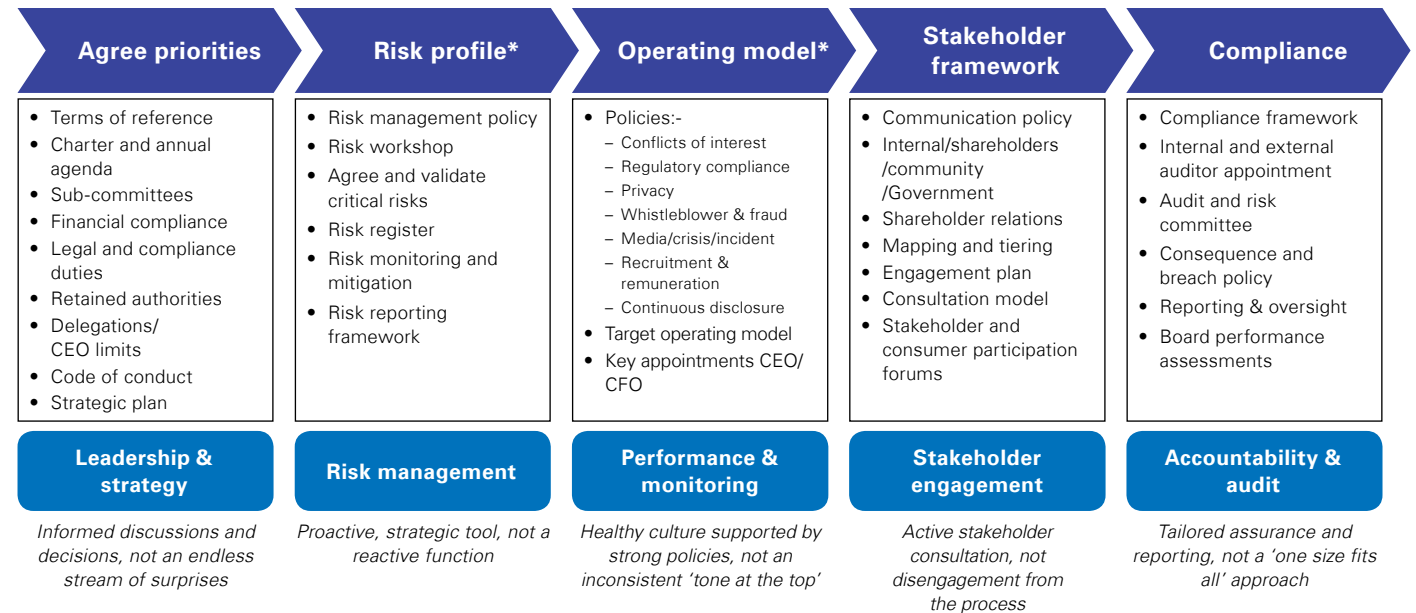
The framework begins by establishing a direction and clear set of priorities for the newly established Board. During this stage, the Board should document its plan and establish timelines and accountabilities around achieving its milestones.

The Board should also then consider its risk management by setting its overall 'risk appetite' and documenting what it considers are the critical risks facing the organisation.

Having the risk appetite established, the Board should then define its target operating model, appoint its key management personnel and approve policies to guide the organisation.

While this is occurring, shareholders and key stakeholders should be engaged.

As part of the final stage in this framework, the Board is also tasked with the role of overseeing the development of an accountability and compliance framework.



\*Note – in practice, it is common for these phases to run in parallel

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
- ▶ 16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

# 16. Managing Cybersecurity Risks

Cybersecurity continues to rise up the board agenda with major incidents increasingly commonplace across a range of industries.

## Questions that company Directors should ask

- |   |  |
|---|--|
| 1. What are the new cybersecurity threats and risks and how do they affect our organisation?  | 4. Are cybersecurity aspects considered in our major business decisions, such as mergers and acquisitions, partnerships, new product launches? |
| 2. Is my organisation's cybersecurity program ready to meet the challenges of today's (and tomorrow's) cyber threat landscape?                    | 5. Is there an ongoing, organisation-wide awareness and training program established around cybersecurity?                                     |
| 3. What key risk indicators should I be reviewing at the executive management and board levels to perform effective risk management in this area? | 6. Are we confident that we will know if we have been hacked or breached, and what makes us certain that we will find out?                     |

## Red flags

- |   |   |
|---|---|
| ▶ Cybersecurity is not on the boardroom agenda  | ▶ Risks associated with cyber threats are not regularly reviewed and updated  |
| ▶ Cyber risk is not specifically included in assessing business and operational risk        | ▶ Organisational strategy and planning does not consider the changing nature of the online world and evolving cyber threats |
| ▶ Specific accountability for cyber risk management, planning, and reporting is not defined |   |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
- ▶ 16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

## Cybersecurity at the heart of your business – more than technology

In a world in which cyber criminals are smart, resourceful and well-motivated, businesses need to make cybersecurity a priority. This cannot be left to the technical specialists in Information Technology (IT) and cannot be addressed in isolation. Cybersecurity, if not already a Board and C-Suite level issue, is destined to become one that will need to be addressed in the context of its wider digital business strategy.

Getting it right will create strategic advantage whilst failure to adequately address the challenge may threaten the sustainability of the business.

By now, corporate boards have woken up to the call that they must address cybersecurity issues at the front line, or business operations as it is not just an IT issue. In fact, cyber risks are an enterprise-wide risk management issue.

An organisation's people, processes and technology working together are key to effective management of cybersecurity risk. Cyber risk management is a fundamental component of governance and must be integrated with supporting activities enterprise wide.

## KPMG's Cyber Maturity framework



KPMG's Cyber Maturity framework is specifically designed to assist organisations in addressing cyber risk by combining the most relevant aspects of international cybersecurity frameworks (National Institute of Standards and Technology ("NIST"), ISO 27001, American National Standards Institute ("ANSI"), SANS, etc.).



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
- ▶ 16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### A robust approach

A robust approach to managing cyber risk, which includes the topic in board level decision making, can reduce volatility and uncertainty, and deliver value right across the organisation by achieving the best possible outcome.

For many businesses, this is an issue that is now rising to the top of the corporate agenda very quickly; it is critical to manage cyber risk in a way that delivers potential competitive advantage rather than impeding growth.

### Boardroom engagement

Boards are getting to grips with the risks that cyber threats pose to their business, both operationally and strategically. Now that almost all organisations include cyber risk in their 'Risk Register', with most of these companies discussing risk at least bi-annually, this awareness should cascade down through their organisations.

While board members are aware of the personal cyber risks they face alongside the corporate threat, too few have a full understanding of the dangers.

Directors who have received no cyber risk training over the past 12 months should be encouraged to sign up for support in the year ahead.

### Understanding what is important

Most boards have a clear, or at least acceptable, understanding of what constitutes their companies' key information and data assets – the crown jewels. But the frequency with which boards review such assets is still too low: most do so rarely or not at all. In today's fast-moving marketplace, an organisation's precious assets

may change quickly, as the business develops new products or services, say, or engages in M&A. Boards need to know what their crown jewels are, where they are, and how they are protected.

### Who leads cyber?

Making it clear who is accountable for any type of risk is a crucial element of good governance. Companies may assign senior responsibility for cyber risk to the CFO, the CEO, or the CIO. Clear cut accountability is essential for effective cyber risk management, but remember that final accountability remains with the board.

***"Executives know that hackers and criminal organisations can wreak havoc on companies; they read about such cases almost every day in the media. But they often don't believe it can happen to them, whether or not they have built defences against the threat."***

Global profiles of the fraudster, KPMG, May 2016

### Critical cyber controls

Organisations can reduce the risks to their business by building up capabilities in four critical areas – prevention, detection, response and recovery.

#### Prevention

Prevention begins with governance and organisation. It is about installing fundamental measures, including placing responsibility for dealing with cybercrime within the organisation and developing awareness training for key staff.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
- ▶ 16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Detection

Through monitoring of critical events and incidents, the organisation can strengthen its technological detection measures. Monitoring and data mining together form an excellent instrument to detect strange patterns in data traffic, to find the location on which the attacks focus and to observe system performance.

### Response

Integrate cyber security response planning into the organisation's overall crisis management program.

Have a well-rehearsed plan to put in place as soon as evidence of a possible attack occurs. During an attack, the organisation should be able to directly deactivate all technology affected.

### Recovery

The incident must be contained and managed before returning to normal operations. The attackers may still be in your network, but your response planning should at a minimum aim to contain the attack and prevent further harm or disruption.

|                                    | Prevention  | Detection   | Response   | Recovery   |
|------------------------------------|---|---|--|--|
| <b>Management and organisation</b> | Appointing cybercrime responsibilities  | Ensuring a 24/7 stand-by (crisis) organisation  | Using forensic analysis skills                         | Establishing criteria for resuming normal operations                     |
| <b>Processes</b>                   | Cybercrime response tests (simulations)<br><br>Periodic scans and penetration tests | Procedures for follow-up of incidents   | Cybercrime response plan                               | Isolation and containment of attacks                                     |
| <b>Technology</b>                  | Ensuring adequate desktop security<br><br>Ensuring network segmentation             | Implementing central logging of critical processes<br><br>Implementing central monitoring of security incidents | Deactivating or discontinuing IT services under attack | Network segmentation and isolation in conjunction with redundant systems |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
- ▶ 16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Attackers

|                  |   |
|------------------|---|
| Insiders         | Someone with knowledge of your organisation and business systems. Insiders may work in collusion with external cyber-attackers or inadvertently disclose sensitive information. |
| Cybercriminals   | Cybercriminals use specialised technology tools to bypass security controls to steal from customers.  |
| Hactivists       | Hactivists are motivated by social or political cause. They are mainly interested in disrupting operations or defacing corporate web pages.                                     |
| State actors     | Government agencies or external parties working for them to steal secrets.  |
| Cyber terrorists | Criminals who seek to cause fear and disruption by spreading malware, bringing down online services and threatening people electronically.                                      |

### Attacks

|                                |  |
|--------------------------------|--|
| Malware                        | Malware includes cyber-attack tools such as computer viruses that attackers use to penetrate your organisation through compromised websites, USB drives and email.   |
| Phishing                       | Phishing emails appear to come from a reliable source and attempt to persuade the victim to reveal sensitive information or to click on a link that will download malware.   |
| Spear Phishing                 | Spear Phishing includes specifically targeted emails that appear to come from a person or organisation that you know and trust. The may direct the victim to make an unauthorised payment, reveal company secrets or download malware. |
| Man in the middle (MITM)       | Attackers position themselves in between the user and a legitimate online site to collect passwords, account details, and personal information.  |
| Key loggers and screen loggers | This is malware that monitors keyboard input in order to fraudulently gain access to passwords and other confidential information.   |
| Ransomware                     | Is a specialised type of malware that encrypts corporate data, making it inaccessible until a 'ransom' is paid to the attackers to make it usable again.   |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
- ▶ 16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Five most common cybersecurity mistakes

*Mistake #1: "We have to achieve 100 percent security".*

*Reality: 100 percent security is neither feasible nor the appropriate goal.*

Almost every large, well-known organisation will unfortunately experience information theft, whether it remains private or is made public. Developing the awareness that 100 percent protection against cybercrime is neither a feasible nor an appropriate goal is already an important step towards a more effective policy, because it allows you to make choices about your defensive posture.

*Mistake #2: "When we invest in best-of-class technical tools, we are safe".*

*Reality: Effective cyber security is less dependent on technology than you think.*

Specialist tools are essential for basic security, and must be integrated into the technology architecture, but they are not the basis of a holistic and robust cybersecurity policy and strategy. The investment in technical tools should be the output, not the driver, of cyber security strategy. Good security starts with developing a robust cyber defence capability.

*Mistake #3: "Our weapons have to be better than those of the hackers".*

*Reality: The security policy should primarily be determined by your goals, not those of your attackers.*

The fight against cybercrime is an example of an unwinnable race. The attackers keep developing new methods and technology and the defence is always one step behind. While it is important to keep up to date and to obtain insights into the intention of attackers and their methods, it is critical for managers to adopt a flexible, proactive and strategic approach to cybersecurity.

*Mistake #4: "Cybersecurity compliance is all about effective monitoring".*

*Reality: The ability to learn is just as important as the ability to monitor.*

Reality shows that cybersecurity is very much driven by compliance. This is understandable, because many organisations have to accommodate a range of laws and legislation. However, it is counterproductive to view compliance as the ultimate goal of cyber security policy. Only an organisation that is capable of understanding external developments and incident trends and using this insight to inform policy and strategy will be successful in combating cybercrime in the long term.

*Mistake #5: "We need to recruit the best professionals to defend ourselves from cybercrime".*

*Reality: Cybersecurity is not a department, but an attitude.*

Cybersecurity is often seen as the responsibility of a department of specialist professionals. This mind-set may result in a false sense of security and lead to the wider organisation not taking responsibility. The real challenge is to make cybersecurity a mainstream approach.

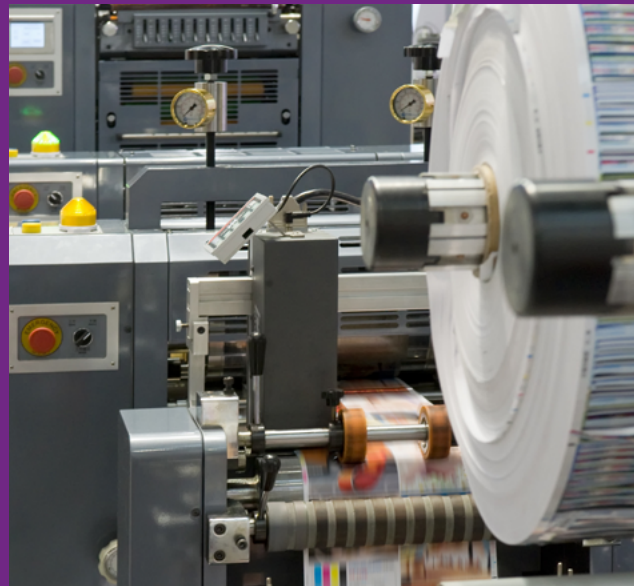
## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
- ▶ 16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices



## Case study: Standard Chartered

In 2013 confidential information about a number of Standard Chartered's Singapore clients was stolen from a printing company, underscoring the vulnerability of global banks to attacks from hackers and thieves. Singapore's central bank took regulatory action against Standard Chartered after reviewing the bank's investigation into the incident.<sup>239</sup>



### Cyber breaches can damage reputation and have wider impacts on confidence

Monthly statements for 647 of Standard Chartered's clients were stolen from the server of Fuji Xerox which provided printing services to the bank. It is not clear how the documents were stolen from the Fuji Xerox server or how they landed on the hacker's laptop.

The security breach threatened to undermine Singapore's reputation as a private-banking and wealth management hub for Asia. Following the incident, shares in Standard Chartered fell to a five-month low in Hong Kong trading.

### Regulatory Sanctions

The MAS announced that it took "appropriate supervisory actions" against the bank and that the regulator "takes a serious view on the safeguarding of customer information, and has reminded all financial institutions to ensure that robust controls are in place, including for operations that have been outsourced to third-party service providers."

<sup>239</sup> <http://www.bloomberg.com/news/articles/2013-12-05/standard-chartered-says-client-banking-data-stolen-in-singapore>



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
- ▶ 16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Cyber Security in outsourcing arrangements

The MAS has issued guidelines and requirements on outsourcing by financial institutions which are currently being strengthened and updated. Any organisation entering into outsourcing arrangements or moving key services to the cloud must ensure that:

1. Risks to business services and sensitive data are clearly understood and documented
2. Security controls to manage those risks are included in service agreements

3. Cyber incident management capabilities are coordinated between the organisation and the service provider
4. The outsourcing or cloud service provider can demonstrate their ability to deliver the required level of cybersecurity controls and incident response.

Organisations can conduct their own reviews of the service provider or assess third party attestations or accreditations to standards such as the ISO 27001(1) international standard on security management, or SSAE 16 (1) and ISAE 3402 (3) attestations.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
- ▶ 16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices



## Case study: Target

In November and December 2013, cyber thieves executed a successful cyber attack against Target, one of the largest retail companies in the United States. The attackers surreptitiously gained access to Target's computer network, stole the financial and personal information of as many as 110 million Target customers, and then removed this sensitive information from Target's network to a server in Eastern Europe.



### Best practices and failure to respond

Target gave network access to a third-party vendor, which did not appear to follow broadly accepted information security practices. The vendor's weak security allowed the attackers to gain a foothold in Target's network.

Attackers who infiltrated Target's network with a vendor credential appear to have successfully moved from less sensitive areas of Target's network to areas storing consumer data, suggesting that Target failed to properly isolate its most sensitive network assets.

Target appears to have failed to respond to multiple automated warnings from the company's anti-intrusion software initially alerting them to the fact that the attackers were installing malware on their systems, and then alerts regarding the escape routes the attackers planned to use to exfiltrate data from Target's network.

### Technology alone is not enough

Six months earlier the company began installing a \$1.6 million malware detection tool also used by the CIA and the Pentagon. Target had a team of security specialists to monitor its computers around the clock and notify Target's security operations centre.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
- ▶ 16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices



## Case study: Target (Cont'd)

On Saturday, November 30, the hackers began to move stolen credit card details and customer personal information to their computers in Russia. The security team notified Target's security operations centre, who for some reason didn't react to the alerts.

When asked to respond to a list of specific questions about the incident and the company's lack of an immediate response to it, Target Chairman, President, and Chief Executive Officer Gregg Steinhafel issued an e-mailed statement: "Target was certified as meeting the standard for the payment card industry in September 2013. Nonetheless, we suffered a data breach. As a result, we are conducting an end-to-end review of our people, processes and technology to understand our opportunities to improve data security and are committed to learning from this experience."

More than 90 lawsuits were filed against Target by customers and banks for negligence and compensatory damages. Total costs were estimated

to run into the billions. Target's profit for the holiday shopping period fell 46 percent from the same quarter the year before; the number of transactions suffered its biggest decline since the retailer began reporting the statistic in 2008.

In March 2014, the Target Board requested CIO Beth Jacob's resignation, followed by Steinhafel's departure in May.

### Boards are accountable for security breaches

*The Target Board was also under significant pressure. A shareholder action firm recommended that investors oust seven board members, contending that the board failed to protect the company from the previous year's data breach. The board members were able to convince shareholders to re-elect them, however, although the message was clear that future data security breaches would be considered to be their responsibility.*

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
- ▶ 16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices



## Case study: Bangladesh Bank

In February 2016, fraudulent instructions to steal US\$951 Million from the central bank of Bangladesh were issued via the SWIFT network. Transactions worth \$81 million succeeded, making this the largest single bank robbery in history. The US Federal Reserve Bank blocked 30 other transactions, amounting to \$850 million, at the request of Bangladesh Bank.



### Attackers exhibited a “deep and sophisticated knowledge of specific operational controls”

Hackers or insiders attempted to steal \$951 million from the Bangladesh Bank's account with the Federal Reserve Bank of New York over two days on which the Bank's offices were closed.

The cyber attackers penetrated Bangladesh Bank's payment systems and payment authorisation codes for the SWIFT international network for inter-bank transfers. Several transfer requests were sent to the Federal Reserve Bank to transfer funds to Sri Lanka and the Philippines. Total losses amounted to \$81 million in transfers to the Philippines which was laundered through casinos. SWIFT revealed that that scheme involved altering SWIFT software to hide evidence of fraudulent transfers, but that its inter-bank messaging system was not affected.

### Attackers at large as attacks continue

In May 2016, SWIFT advised of another attack against an unnamed commercial bank. Forensic experts linked the Bangladesh Bank attack to a wider campaign targeting banks globally. SWIFT acknowledged that the Bangladesh Bank attack was not an isolated incident but one of a number of recent criminal schemes aimed at its messaging platform, which is used by 11,000 financial institutions globally.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
- ▶ 16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices



## Case study: Bangladesh Bank (Cont'd)

### Cyber attacks are increasingly more sophisticated

Cyber attackers have grown far more sophisticated over the past 5 years, learning how to infiltrate corporate networks and financial systems without being detected and subsequently inflicting millions of dollars in losses due to theft and damages caused.

Since late 2013, an unknown group of hackers dubbed the Carbanak Gang has reportedly stolen \$300 million - possibly as much as triple that amount - from banks across the world.

### Developing a cyber resilience capability

Expert skills and advice and special technology tools are certainly required, but a key element to developing

and maintaining a successful cyber resilience capability is effective corporate governance and board oversight to ensure that:

- Cyber risks are clearly understood
- Appropriate advice and skills are available to address those risks
- Your staff and management are aware of their responsibilities and trained to recognise cyber threats
- Critical technology systems are monitored and protected
- You have a well developed and tested cyber security strategy and incident response capability.



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
- ▶ 16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Action steps for implementing a cybersecurity governance plan

No two corporations are the same, therefore there is no 'one-size-fits-all' cybersecurity action plan. Some firms still have to take first basic steps, others have launched initial efforts to address cybersecurity concerns, and a few firms have implemented robust management and response plans, but there is going to always be room for improvement.

No matter where your organisation falls on the spectrum, one thing is for certain—it takes much more than just an IT tool to batten down the security hatches. Effective management of cybersecurity requires a company-wide effort, with detailed plans and processes. There are some key governance related elements to visit and continuously revisit as this environment evolves.

### Alignment with business strategy

Companies are increasingly taking cybersecurity seriously, but too often their efforts are not coherent with their overall business strategy. Many companies fail to ask themselves: 'What are we trying to achieve as a business, and what are the cyber threats to those objectives that we need to counter?'

Cyber risk is an important strategic concern for Boards. Its true nature is dependent upon external threat actors as well as industry sector, business activities and corporate objectives.

A clear linkage between business objectives, the threats to those objectives, and the enabling security capabilities to counter the threats, makes the investment decision easier and it becomes a straightforward balance between Return on Investment and residual risk.

Without a clear strategy and roadmap, people look for the latest, greatest thing being promoted in the market. Companies end up focusing disproportionate resource into the implementation of expensive technology solutions – viewing them as some kind of universal panacea for any security fears – rather than emphasising skills and awareness, or focusing on targeted security investments to enable business change.

### Critical success factors:

- The roles of directors and the board in managing and overseeing cybersecurity and cyber incident response are clearly defined and documented
- Accountabilities and reporting lines for cybersecurity management are clearly defined and well understood
- There is regular enterprise-wide cyber risk communication
- We have a comprehensive awareness framework that focusses on effective communication throughout the organisation
- We are addressing the key issues and ensuring that staff at all levels are receiving clear and relevant messages
- The key issues and concerns around cybersecurity are clearly communicated in our meetings, our directions, and in communication from management
- We receive the right reports and information we need to effectively manage cybersecurity risks
- We are transparent in informing our stakeholders about cyber risk and security concerns.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
- ▶ 16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Useful references

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- Singapore Cybersecurity Masterplan 2018 <https://www.ida.gov.sg/~/-media/Files/Programmes%20and%20Partnership/Initiatives/2014/ncsm2018/NationalCyberSecurityMasterplan%202018.pdf>
- Empowering Your Cyber Security: <http://www.kpmg.com/SG/en/IssuesAndInsights/ArticlesPublications/Documents/Advisory-CS-Empowering-Your-Cyber-Security.pdf>
- Cyber security for audit committees. <https://www.kpmg.com/PL/pl/IssuesAndInsights/ArticlesPublications/Documents/2014/Cyber-Security-for-Audit-Committees.pdf>
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- Cyber threat intelligence and the lessons from law enforcement <https://www.kpmg.com/SG/en/IssuesAndInsights/ArticlesPublications/Documents/Advisory-CS-Cyber-threat-intelligence-and-the-lessons-from-law.pdf>
- Cyber Security Dashboard: Monitor, Analyse and Take Control Of Cyber Security <https://www.kpmg.com/NL/nl/IssuesAndInsights/ArticlesPublications/Documents/PDF/IT-Risk-Advisory/Cyber-Security-Dashboard1.pdf>
- Cyber security: a failure of imagination by CEOs) <https://home.kpmg.com/xx/en/home/insights/2015/12/cyber-security-a-failure-of-imagination-by-ceos.html>

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
- ▶ 17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

# 17. Corporate sustainability

As part of the new SGX sustainability reporting requirements, companies will have to identify and report on their material ESG factors, set out policies in relation to the factors identified, set performance targets for them for the forthcoming year, and select a globally-recognised framework to report on them on a comply or explain basis. Overall, the Board holds ultimate responsibility for sustainability and its reporting.

## Questions that company Directors should ask

- |   |  |
|---|--|
| 1. Is the Board aware of the company's material environmental, social, and governance ("ESG") risks and opportunities?                              | 5. Has the Board received appropriate training to be able to understand and challenge senior management on the strategy, relevance, and performance of ESG matter and risks? |
| 2. Is the Board aware of its roles and responsibilities in relation to these issues and which committee is responsible for oversight and reporting? | 6. Does the Board have visibility over the company's strategy in relation to its corporate sustainability initiatives?   |
| 3. Is there a governance framework in place for managing ESG issues? Does responsibility lie with a 'C-Suite' executive?                            | 7. Does the company report publicly on its ESG strategy, performance, governance and risks and does the Board sign off the report prior to publication?                      |
| 4. Does senior management report to the Board on ESG issues and are ESG targets aligned to broader business objectives?                             | 8. Is the Board aware of the likely costs of non-financial impacts and potential mitigation strategies? Does the organisational strategy consider these impacts?             |

## Red flags

- |  |  |
|--|--|
| ▶ An absence of ESG considerations in the overall strategic business objectives  | ▶ ESG incidents occur with little warning and are dealt with passively                           |
| ▶ ESG issues and costs are rarely reported, discussed or considered at Board level, or publicly disclosed as part of the company reporting process | ▶ Sustainability is mentioned to please external stakeholders but is not adopted internally      |
| ▶ No executive is accountable for ESG issues and no clear governance structure is in place   | ▶ The sustainability team spend most of their effort collecting data, but little action is taken |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
- ▶ 17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

## The broader context

The prevalence of corporate sustainability as a mainstream issue is evidenced by the emergence of integrated reporting, new regulatory requirements and the active involvement of the investment and analyst communities. The role of directors in this space is also evolving; it can no longer be ignored.

Growing stakeholder awareness, particularly in the investment community, is driving organisations to consider and address the ESG issues within their business. These non-financial risks are now having significant financial implications and, therefore, disclosure expectations with respect to the management and performance of material environmental and social issues are also on the rise.

The SGX Sustainability Reporting Guide ("the Guide") recognises the increasing calls globally for the business community to address the effects of ESG responsibility. As such, it requires companies to identify the material ESG factors, and describe both the reasons for and the processes of their selection<sup>237</sup>. For better integration within the company's structure, this includes taking into consideration their relevance to the business, strategy, business model, and key stakeholders. Further, it requires that companies need to select a Sustainability Reporting ("SR") framework and disclose the rationale for its selection as well as the extent of the framework's application.

The key with regard to reporting ESG factors is the disclosure of how these factors contribute to the creation of value for the company. A risk ranking and prioritisation process will allow for their distillation and eventually integration into the firm's Enterprise Risk Management ("ERM") process. Finally, the Board should determine the material ESG factors and the issuer's response to the attendant risks and opportunities.

## Key concepts

Institutional investors and analysts are today commonly applying ESG factors in their assessments of the long term performance of companies. ESG covers a broad range of business issues relating to the ongoing sustainability and ethical impact of a company, such as human rights, climate impacts, stakeholder relations and links between remuneration structures and shareholder returns. As investors increasingly look to a firm's social and environmental performance in addition to its economic performance ESG now is an additional decision making criterion for investors.

237 Section 4.1. i, of the SGX Sustainability Reporting Guide, 20 June 2016

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
- 17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices



## Case Study<sup>238</sup>

Sustainability data is now becoming the norm in investment decision making processes. Organisations may miss out on securing investment if they are unable to meet the specific sustainability criteria set by investors. For example, Norway's Government Pension Fund Global (GPF), the world's largest sovereign wealth fund, has dropped 11 companies because of connections to deforestation, the Fund stated in its 2015 Annual Report. Four firms were formally excluded by the Fund's Council on Ethics after investigations showed that their palm oil plantations caused serious environmental damage in Indonesia, including fires in at least one case.



As one of the leading global institutional investors, this move is reflective of the increasing focus and influence of sustainability in investment decisions. The general momentum of proponents such as the UN Principles for Responsible Investment ("PRI") further attests to this movement.

The investor-driven ESG overlay on corporate financial performance, as seen through the corporate lens, is the concept of externalities. An externality is a side effect or 'spill-over' impacting a third party resulting from a profit-driven decision which the company has not taken into account. Externalities, such as emissions or safety procedures in the supply chain, may be ignored by companies in the quest for short-term profitability, but in the medium-term are likely to erode shareholder value. The challenge for companies is the extent to which they 'internalise externalities' in their day-to-day and strategic decision making.

ESG issues and externalities are often difficult to quantify, and are, therefore, commonly generically referred to as non-financial factors or risks.

<sup>238</sup> <http://www.straitstimes.com/asia/se-asia/norway-fund-drops-11-firms-over-deforestation>



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
- 17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

### Drivers

The key drivers behind the internalisation of the sustainability 'mega-forces' are:

5. increasing stakeholder pressures
6. regulations and standards
7. market dynamics.

Just as the mega-forces underlying them are interconnected, so are the three drivers of internalisation. For example, stakeholder pressure (such as public protest) can encourage regulators to create or strengthen legislation which, in turn, changes market dynamics. Market dynamics (such as resource shortages) can trigger stakeholder pressure such as community unrest, which can prompt authorities to legislate.

The pressure to transparently demonstrate how ESG assessment criteria are utilised across governance, processes and reporting is largely due to stakeholder demands to understand more about the sustainability of a company and its key decisions. The power of stakeholders has grown exponentially with the rise of social media and the knowledge is shared globally almost instantly.

Investors and analysts are the stakeholders with the most direct impact on companies, but the indirect impacts are continuously growing stronger. Much of the value of companies today is inherent in intangible assets, such as brand names and reputation rather than traditional tangible assets. These intangible assets are closely linked to ESG factors and their value can be readily destroyed if these factors are not managed.

### SUSTAINABILITY MEGA-FORCES



### DRIVERS OF INTERNALISATION

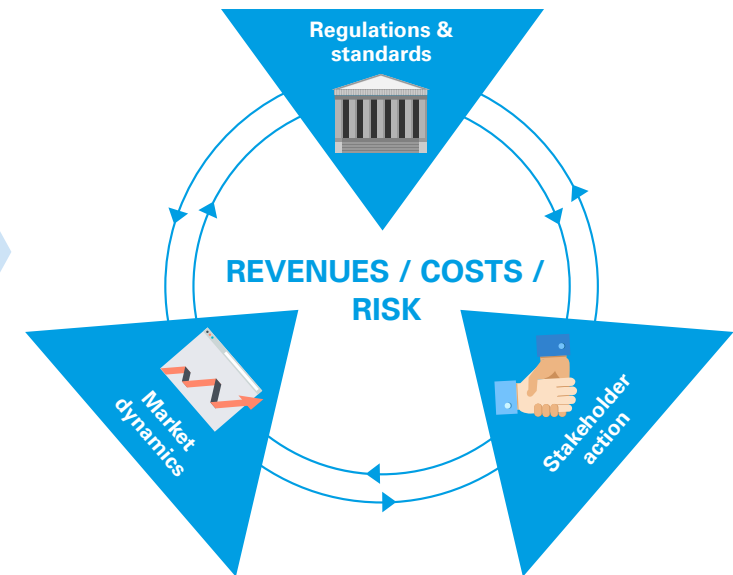


Figure 1: The interplay of global drivers of sustainability and its integration in the corporate context;  
Source: KPMG, A New Vision of Value, 2014

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
- 17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices



## Case Study<sup>239</sup>



239 <http://www.businessinsider.com/how-nike-solved-its-sweatshop-problem-2013-5?IR=T&>

Nike had received unfavourable media exposure in relation to labour practices since the 1990s – low wages, poor working conditions, and the use of child labour. Nike countered this by increasing minimum wage rates, the minimum age requirements of workers, performing audits on their factories globally, and working with NGOs to actively monitor factories. Subsequently in 2005, Nike became the first in its sector to publish a report on wages and working conditions in their factories, and continues to post its commitments, the standards it complies with, and audit data in its corporate responsibility report.

This example demonstrates how Nike managed the social issues affecting its operations and was then able to rebuild its brand and reputation.

There are also a growing number of regulatory recommendations driving the increased focus on ESG issues, such as the Guide, which require listed companies to comply or explain with regard to their application. In addition the UN Sustainable development goals, and signatory requirements under the PRI provide global better practice guidance.

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### ► 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### 21. Appendices

## Strategy

At the heart of a firm's business operations lies its strategy which is summarised and communicated to the broader stakeholder community through the business vision. To ensure that sustainability has credibly been considered as part of the Board's strategic formulation it should be integrated as part of this strategy. This process begins at the materiality determination phase.

1. The first step where the Board needs to exert its influence and carry out its sustainability duty is the determination of those ESG factors identified as material. This requires the Board to:
  - Have oversight over the determination process involved in deriving said material items through discussion with management. It also requires the Board to approve the justification as to why they are material.
2. Once the material factors have been identified these may be aligned with stakeholder's expectations and requirements. This requires the Board to:
  - Have visibility of the selected stakeholders and approve their mapping, tiering, and profiling.
  - Have oversight of the modes of engagement and stakeholder feedback provided.

Delegate stakeholder engagement to senior management to form part of the materiality determination process which may be linked to the development and reiteration of the firm's strategy.

Decisions as to the extent of accounting for a firm's negative external impacts across the value chain should be taken at Board level within an organisation, applying a risk management approach to minimising potential future costs and promoting the long-term sustainability

of the organisation. At face value, ESG risks are largely non-financial, however, social and environmental issues inevitably result in economic impacts; it's just a matter of timing.

Key to understanding non-financial risks is the integration and impact of these risks on the economic success or failure of an organisation, including:

- regulatory risk due to complex changes to the regulatory landscape
- reputational risk and damage to corporate reputation and value through adverse publicity
- competitive risk from fast changing market dynamics, uncertainty of supply, and price volatility of key inputs
- exposure to legal action through, for example, non-disclosure of environmental, social and governance information.

Oversight of the effective management of non-financial risks and opportunities is the responsibility of the Board, and an increasing number of stock exchanges and Governments alike are seeking more public disclosure on ESG governance in recognition of this responsibility. A Board should consider the relationship between non-financial and financial risks, and whether these are adequately identified and addressed by the company.

The SGX guidelines suggests that listed entities have processes in place to address both ESG risks and opportunities as these have direct bearing on strategies and operations and should be reported for clearer understanding of the issuer's performance, prospects and management quality<sup>240</sup>.

240 Recommendation 3.3 of the SGX Sustainability Reporting Guide, 20 June 2016

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
- ▶ 17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

Effective oversight of an ESG framework also requires consideration and challenge on the extent of ESG integration into corporate strategic planning, both in the short and long term. The Board should ensure the ESG issues identified as most material to the organisation are connected to existing strategy and risk management processes. An adequate ESG governance structure will be helpful in ensuring this.

However, focusing exclusively on the ESG risks would deprive companies of many benefits that could arise from product and process innovations around sustainability. Examples of such opportunities include Clorox which in 2008 launched a line of non-synthetic cleaning products known as Green Works. By the end of 2008 Green Works had grown the U.S. natural cleaners market by 100%, and Clorox enjoyed a 40% share of the \$200 million market<sup>241</sup>.

## Materiality and risks

Effective ESG risk management requires a robust mechanism for the identification and assessment of issues that are material to the organisation. This process is known as the materiality determination process and entails the following 7 steps:

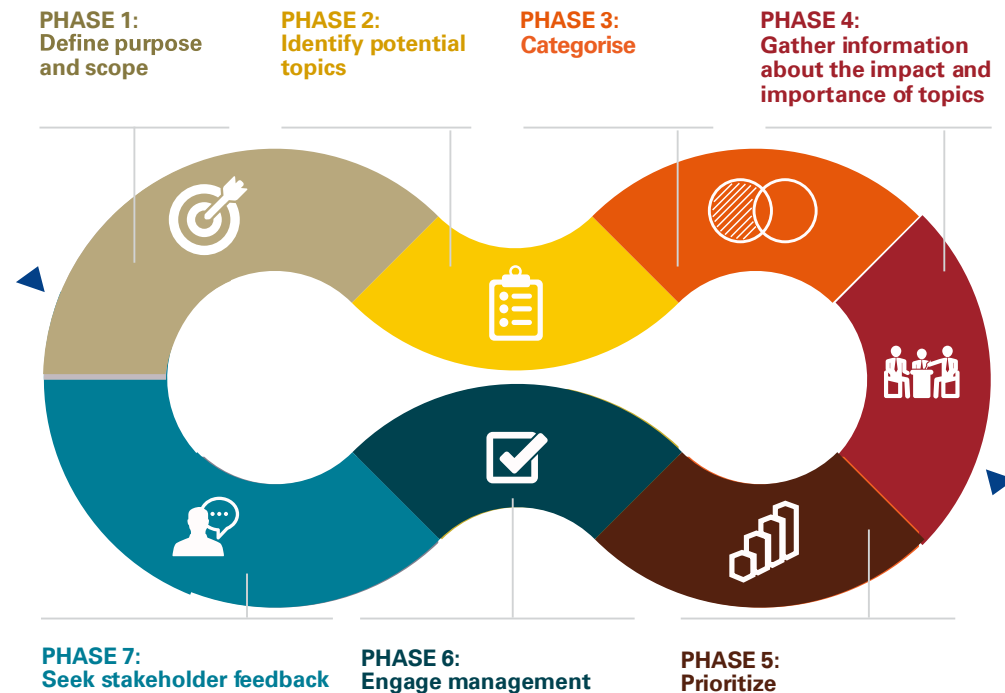


Figure 2: Materiality determination process

241 Sustainability is now the key driver of innovation, Harvard Business Review, <https://hbr.org>

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
- 17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices



### Environmental

- Water consumption
- Energy consumption
- Emissions
- Effluents & Waste
- Nutrition
- Food safety
- Materials



### Social

- Occupational Health & Safety
- Human Rights
- Community Involvement & Investment
- Fair Trade & Labour Relations
- Rural development
- Staff Development
- Employment
- Non-discrimination
- Anti-corruption & anti-fraud



### Governance

- Corporate Vision
- Innovation & Productivity
- Customer Satisfaction & Awareness
- Sustainable Supply Chain
- Products development
- Risk management & corporate governance
- ERM & ESG governance structure
- Technology & Security
- Business opportunities, growth, and diversification

Figure 3: Common examples of material ESG factors

Material factors identified during the process should be disclosed in the report. Figure 3 above illustrates an exemplary overview of potential material ESG factors commonly found across industries.

Materiality with respect to ESG risks does, however, involve a more qualitative assessment of issues than is traditionally applied in financial reporting. The Guide defines material exposure as 'the most important ESG risks and opportunities that will act as barriers or enablers to achieving business goals'<sup>242</sup>

Material sustainability matters for individual organisations are likely to be similar within sectors, however, there may be instances where these can differ. Factors contributing to the determination of material sustainability matters may include the business model and strategy, products and services, types of stakeholders, size of the organisation, geographical presence, and the organisation's risk appetite, etc. Therefore, you should apply materiality based on your own set of circumstances.

242 SGX Sustainability Reporting Guide, 20 June 2016



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
- 17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

When applying materiality, companies may consider formulating criteria to determine what is significant or substantive. The criteria that you could consider adopting to determine if ESG impacts are significant, or if the matter substantively influences stakeholders' assessments and decisions may include, among others, the severity and likelihood of the impacts over time on financial performance, actual or perceived value of the organisation, availability of products/services or reputation.

This kind of prioritisation is best done in the form of a materiality matrix which combines both materiality considerations with stakeholder feedback.

### Applying materiality across organisational value chain

In applying materiality, you are encouraged to closely consider all parts of your organisation's value chain. This simply means considering more broadly the impacts of your products and services beyond your operations. For example,

- once your product has left the production line, does it contribute to negative impacts (e.g. excessive consumption of electricity due to inefficiency) during the course of its usage?
- can opportunities be created through the management of such a risk (i.e. product redesign using less packaging, which in turn could drive cost efficiencies)?

Sometimes the smallest part (either financially or physical operations) of your business can pose the most significant ESG risk. Therefore, you should also consider the nature of your operations (e.g. use of hazardous chemicals) and its location (e.g. remote locations or countries with poor sustainability-related legislation and inadequate enforcement), in addition to its size in applying materiality.

Directors should enquire of management whether a robust materiality assessment process and ESG risk assessment are in place, and how key non-financial and financial risks interact across their business. This includes understanding where the key non-financial exposures are across the organisations' value chain and the potential subsequent cost/impact, such as costs arising from the impact of extreme weather events and reputational damage associated with human rights issues/claims. This assessment may also identify economic opportunities across the environmental and social impacts observed.

Identifying and understanding the material ESG issues, and the risks and opportunities they represent, is a critical part of promoting the long-term sustainability of the organisation. The Board should enquire of management whether there is strong alignment between the materiality assessment process for ESG issues and the organisation's existing risk management and strategy development processes.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
- 17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices



## Case Study<sup>243</sup>



As companies' financial performance is significantly impacted by non-financial matters such as environmental and social performance, accounting for their impacts on the firm's economic performance will allow for the realisation of additional value.

One current example would be a major Singapore-based supermarket chain that reviewed its suppliers in light of the haze situation. This resulted in the exclusion of all haze and 'slash and burn' deforestation related products. Any firms impacted by the haze could have avoided this situation had they had an ESG strategy and risk management system in place and processes that would have let them proactively avoid such an outcome as opposed to just reacting to it.

<sup>243</sup> <http://www.straitstimes.com/singapore/environment/ntuc-fairprice-sheng-siong-prime-supermarket-remove-all-asia-pulp-paper-group>

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
- ▶ 17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

## Role of the Board

The Board plays a key role in leading a company's commitment to ESG issues and their consideration and integration across the organisation. This can be done by:

- recognising responsibility for ESG issues at Board level and ensuring that ESG governance is appropriately delegated across the organisation
- providing clear strategic direction on ESG issues for the short and long term in order to allow for the development of a more detailed ESG framework
- monitoring the assessment and regular review of material issues
- oversight and challenge of management's financial and non-financial assessment of material risks
- challenging the performance of the company in relation to ESG targets and related KPIs
- establishing a corporate culture that supports the effective management of ESG related issues, in recognition of their importance to the long-term sustainability of the organisation
- oversight of the depth and breadth of ESG-related reporting and the alignment with recognised frameworks and initiatives
- requiring senior management approval and external assurance over ESG reporting in order to ensure confidence in the information and the business systems and processes from which it is sourced
- undertaking training to keep up to date with the evolving issue of ESG and to be able to lead and challenge management
- integrating the sustainability strategy into the overall business strategy.

## Governance and culture

In order to give life to the sustainability strategy, it needs to be anchored in the company's governance structure. The close interaction with senior management will enable the Board to satisfy itself on the way ESG governance is structured and functioning through the various management levels.

1. The first step involved in ensuring effective governance structures are in place is to assign responsibility for them at Board and management level.
2. The Board should also gain oversight of any ESG policies in place as these are what is used to embed the sustainability strategy in the business model. In their absence, management needs to be tasked with overseeing policy drafting and roll-out.
3. The Board is also responsible for ensuring sustainability is being reflected in the firm's daily operations.
4. Finally, the Board needs to satisfy itself that controls over monitoring and managing sustainability in the firm's daily operations are working effectively.

The successful implementation will also entail the integration of any identified material ESG risks and opportunities within the company's ERM system.

To ensure that ESG risks are monitored adequately the Board needs to:

- Gain oversight of ESG risks and opportunities and ensure integration into firm's ERM framework is in place
- Understand how ESG risks and opportunities are embedded into the firm's strategy and reflected in its business model
- Ensure management takes proactive measures to manage and mitigate reputational risks arising from ESG factors.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
- 17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

Effective management of non-financial risks and opportunities also requires a robust governance structure. The ESG framework should detail the governance arrangements in place to oversee the effective identification and management of ESG risks across the business, setting the tone at the top for the rest of the organisation.

The Board is ultimately responsible for the oversight of risk, although the Board may delegate this to the Board committee responsible for the oversight of ESG matters. Regardless of the approach, clear reporting lines and responsibilities should be established and communicated. Some companies are choosing to set-up a specialised committee to oversee non-financial matters. Figure 4 below provides an illustrative sustainability governance structure.



Figure 4: Illustrative Sustainability Governance Structure

It is the responsibility of directors to ensure they receive adequate and appropriate training and continuous development in order to ensure they are fully equipped to carry out their roles, make informed decisions, and adequately challenge management in the area of ESG risk management.

Boards are increasingly expected to promote and support a corporate culture which embeds the consideration of

environmental and social issues into decision-making and performance throughout the organisation. The ESG governance framework should include clear expectations of how risk and opportunities are managed and who within the organisation is accountable. Raising the visibility and importance of the issues through specific KPIs for senior management that cascade down the organisation, is one way the Board can set the tone and influence corporate culture.



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
- 17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices



## Case Study<sup>244</sup>

Singapore-based City Developments Limited (CDL) ensures that sustainability has the attention of its Board, with the CEO as the primary focal point. The Corporate Sustainable Development department under the responsibility of the CSO, reports directly to the CEO. Finally, the CSR committee is represented across all business and operational units of CDL.



244 City Developments Limited (CDL) Sustainability Report 2016

## KPIs and Metrics

An effective way for directors to assess progress against identified material risks is to ensure management implement targets and KPIs associated with each material indicator. It is the responsibility of directors to ensure that management has implemented systems, procedures and controls to gather reliable and timely information about key environmental and social trends and issues.

Directors should understand and agree on management's selection of key performance indicators regarding environmental and social performance, and ensure periodic reviews take place of company and individual performance against these indicators. The Board and management should engage in discussions over the types of performance indicators that need to be set, measured, rewarded and communicated. The indicators selected for assessment should be based on appropriate data collection and reporting systems, and, most importantly, should be relevant to the company's material ESG issues identified through its materiality assessment.

Overall an effective approach to performance measurement entails:

- a) Measurement and reporting of relevant and contextual information as opposed to non-meaningful incomparable data is important: Emissions per \$ of revenue as opposed to absolute emissions.
- b) Finally, engaging in meaningful measurement of value creation by assessing the positive impacts the firm made through its environmental and social performance. This allows the firm to effectively communicate its long-term value creation.



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
- 17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices



## Case Study<sup>245</sup>

Mirvac, a property development company in Australia, wanted to understand the value they are creating in society through their business activities. Along with KPMG Australia they embarked on an industry first and created a framework for measuring their social and economic impacts. For example, by incorporating more open spaces, they encouraged more connectivity, community engagement and social cohesion, which led to an increased feeling of safety and a reduction in crime. Mirvac were able to measure the value of this reduction in crime to be worth \$108 - \$493 in social value per year, per residence. They also discovered that just a 1-unit increase in expenditure on parks and recreation resulted in a 26 unit reduction in crime. This social impact measurement has helped Mirvac understand, in tangible terms, the positive impact they have on their customers, partners, and their own business. Furthermore, this tool can be used in the future to measure the likely social impact of new developments.



245 The Value of Community – “Understanding our social return on investment”, by Mirvac, 2016

## Useful references

- KPMG, A New Vision of Value, 2014, <http://www.kpmg.com/au/en/issuesandinsights/articlespublications/pages/new-vision-of-value.aspx>
- KPMG, Currents of change, Corporate Responsibility Reporting Survey, 2015, <http://www.kpmg.com/cn/en/issuesandinsights/articlespublications/pages/kpmg-survey-of-corporate-responsibility-reporting-2015-o-201511.aspx>

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
- ▶ 18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

# 18. Social media

In this hyper-connected world, the explosion in social media use has resulted in an empowered consumer. This empowered consumer, along with the convergence of social and traditional media, has introduced contemporary risks that many 'traditional' risk management frameworks are not equipped to deal with.

## Questions that company Directors should ask

- |  |  |
|--|--|
| 1. Has a review been done to identify and understand potential social media risks facing the organisation?       | 8. How literate is the Board with respect to the use of social media?  |
| 2. Does the organisation have a documented framework for identifying, mitigating and managing social media risk? | 9. Is there a social media plan in place?  |
| 3. Has the organisation identified the possible exposures that it may face from social media?                    | 10. Has an analysis been undertaken to identify key influencers and stakeholders for the business in the social media landscape? What proactive engagement strategies are in place to manage these stakeholders? |
| 4. Has a review of the possible impacts of social media on the supply chain been undertaken?                     | 11. Is the organisation making the optimum use of social media?  |
| 5. What social media regulations are in place for our industry and have they been considered?                    | 12. Has the organisation considered how key competitors are using social media?  |
| 6. Is there a single point of accountability for social media risk?  | 13. Has the organisation reviewed all social media channels to determine what is being said about it?  |
| 7. How is social media risk reported to the Board?   |  |

## Red flags

- |  |  |
|--|--|
| ▶ Lack of recognition that social media is a risk  | ▶ The organisation does not embrace the many benefits of social media  |
| ▶ Little understanding of the underlying risks stemming from social media beyond reputational risk           | ▶ No expansion of customer service, investor relations or public affairs into the social media operating framework |
| ▶ No formalised social media monitoring or reporting in place that extends beyond the 'Marketing Department' | ▶ Lack of innovation to see social media as more than a 'campaign' tool  |
| ▶ Limited social media governance frameworks   | ▶ Reporting is limited to 'vanity metrics' such as the number of Twitter followers or Facebook page 'likes'        |
| ▶ Frequent social media mishaps or gaffes occurring  |  |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
- ▶ 18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

Social media is not a fad. It represents an evolution in technology use and is now an undeniable factor in modern society. The historical approach of many organisations blocking social media access during work hours and choosing to not participate in the medium is no longer a mitigation tactic, but a liability, and, an extremely risky approach. Perhaps the most compelling statistic for company directors is the adoption of social media by Fortune 500 corporations – 70 percent have Facebook Pages, 77 percent have a presence on Twitter and 69 percent are posting material on YouTube.<sup>246</sup> Furthermore, the shifting power structure of the media has made social media a driving force behind activism directed at companies and their leaders.

The view of many directors regarding social media is limited to a narrow debate about the technology itself and within the context of 'marketing', or alternatively, about how little it has impacted their business. Unfortunately, this perspective does not address the reality of the situation. We are witnessing a large scale transformation driven by "a growing tension between two distinct forces: old power and new power<sup>247</sup>". Old power business models which are based on consumption and require little to no involvement from the buyer or consumer, whereas new power is 'made by many', is participatory and peer-driven. This is all happening as a result of the mass adoption of social media.

If a director is in an industry that is being disrupted or impacted by any form of digital technology, whether directly or indirectly, then it is not simply enough to address the problem with a 'Facebook Page'. This is akin to painting a house with faltering foundations. In this new

social environment, Directors must understand the real world impact that the new social media power paradigm brings. One clear example of this is the growing influence of activism that companies, at any point in a supply chain or project, can experience.

### Social media risks

When used positively, social media can provide an organisation with a range of exciting and powerful opportunities to create and connect with markets and stakeholders. However, for many organisations, it continues to present a variety of risks. These risks go way beyond the typical 'customer complaint' being posted to a company Facebook Page. The interconnectedness of the traditional and social media has amplified the velocity and strength of a single 'tweet' to the point where it can now move global share markets and can even be used to manipulate the share price of an individual organisation. For example, in April 2013, a group hacked the Associated Press Twitter account and tweeted that a plane had crashed into the White House. The effect? The stock market dropped nearly almost 150 points in a matter of minutes.<sup>248</sup>

In essence, there are two key aspects to social media risk – the controllable organisational use and the uncontrollable external landscape. Internal or organisational social media use (i.e. how social media is used within the organisation) without a proper strategy, governance framework and control structure in place can potentially expose an organisation to increased regulatory, reputational, legal and financial risks. Whereas, social media users and participants external to the organisation

<sup>246</sup> Social Media Use Growing Among Fortune 500, Amy Gesenhues, Marketing Land, July 2013

<sup>247</sup> Understanding New Power – Harvard Business Review, December 2014 (Heimans and Timms)

<sup>248</sup> The Guardian (2013, 24 April). AP Twitter hack causes panic on Wall Street and sends Dow plunging. Retrieved from <https://www.theguardian.com/business/2013/apr/23/ap-tweet-hack-wall-street-freefall>

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
- ▶ 18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

present a variety of unknown and constantly evolving risks, ranging from fraud to supply chain disruption. Social media has evolved faster than most organisations' risk management frameworks – compounding the need to put in place appropriate protocols, procedures and knowledge.

Social media has allowed for an unprecedented ability to gather information and communicate to mass audiences. The key risk is for stakeholders to locate one-another, connect and cooperate to achieve disruptive ends.

It is the role of directors to ensure that they remain aware of the changing social landscape and the issues that can potentially turn into major crises for the organisation in a matter of minutes. This involves undertaking their own research (media scans), engaging with stakeholders and challenging management on the corporate risks brought to the Board for review.

Useful questions that the Board could ask themselves before introducing the use of social media:<sup>249</sup>

- What social media platform are most effective?
- What are the best ways to engage my audience with social media (e.g. chat rooms, hashtag, etc)?
- How do I measure the return on my social media marketing?
- What are the best social management tools?
- How do I find my target audience with social media?

### Stakeholder activism and social media

Boards are no doubt aware of the significant influence that stakeholders have over their business. Increasingly, social media platforms are being used by stakeholders to agitate, or lobby, for attention on a whole range of issues.

One of the leading social media risks stems from the capacity of social media to be used by key stakeholders to agitate for change in a very public and often rapid manner.

Shareholders are key stakeholders and are increasingly active through social media and direct engagement with the organisation. Shareholder activism can occur from different ends of the investor spectrum:

- Wealthy and influential investors with large stakes influencing the public perception of the share price and advocating for changes to company operations through social media.
- Small shareholders using their position to advance their credentials and earn a platform to promote change.

The prominent US billionaire investor Carl Icahn is often a key exponent of shareholder activism. In January 2014, Mr Icahn was reported to have used his position as an eBay shareholder to lobby for the development of a new electronic payments method which would separate the company from its long-term relationship with PayPal.

In May 2015, Gushcloud and Singtel came under fire for a negative ad campaign that centred on social media influencers posting negative reviews of Singtel's competitors - Starhub and M1. The Infocomm Development Authority of Singapore (IDA) issued a stern warning to Singtel regarding this negative marketing campaign.<sup>250</sup> Even though there is no specific Act that explicitly governs social media, it can be said that authorities are aware and have little tolerance for misuse of social platforms.

<sup>249</sup> Social Media Singapore 2015 [Infographic]. Retrieved from <http://www.hashmeta.com/social-media-singapore-infographic/>

<sup>250</sup> AsiaOne (2015, May 22). Singapore's social media marketing company Gushcloud in multi-million dollar deal. Retrieved from <http://news.asiaone.com/news/business/singapores-social-media-marketing-company-gushcloud-multi-million-dollar-deal>

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
- ▶ 18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

Social media also impacted the Singapore General Election in 2011 when the People's Action Party ("PAP") announced a new young candidate, who immediately created a lot of negative sentiment on social media through aspects of her personal life and potential unsuitability to be a Member of Parliament ("MP"). As a result, although she won the seat, the poor election poll in the area was linked, either directly or indirectly, to this publicity.<sup>251</sup>

Similarly, the 'Stop Lynas' campaign waged through social media, brought the rare earths mine run by Lynas in Malaysia to a halt, and led to significant financial costs being incurred by the company as a result of the delays. As Lynas Corp. Chief Executive Officer Nicholas Curtis said in an interview with Bloomberg, "he underestimated the power of Facebook and Twitter when his mining company decided to build the world's biggest rare-earths plant in Malaysia".<sup>252</sup>

In 2014, Tan Tock Seng Hospital (TTSH) was forced to defend its hiring policy for foreign workers after a nurse posted racist and inflammatory comments on Facebook that specifically targeted Singaporeans. The subsequent backlash on social media lead to the dismissal of the staff member and TTSH had to publicly defend its staff values of respect, professionalism and social responsibility, and its ratios of foreign workers.<sup>253</sup>

251 AsiaOne. (2011, March 31). PAP's youngest candidate faces online criticism. Retrieved from <http://news.asiaone.com/News/AsiaOne+News/Singapore/Story/A1Story20110331-271039.html>

252 Porter, B. & Permatasari, S. (2012, July 2). Lynas CEO Finds Social Media Hobbles Rare-Earths Plans. Bloomberg. Retrieved from <http://www.bloomberg.com/news/articles/2012-07-01/lynas-ceo-finds-social-media-hobbles-rare-earths-plans>

253 Hoe, P S. (2015, January 9). Tan Tock Seng Hospital fires Filipino nurse who made offensive comments on Facebook. Straits Times. Retrieved from <http://www.straitstimes.com/singapore/tan-tock-seng-hospital-fires-filipino-nurse-who-made-offensive-comments-on-facebook>

The above examples demonstrate the need for directors to not only be aware of stakeholder influences, but also to ensure that there are robust frameworks in place to protect and create organisational value through robust risk management frameworks and social media policies or protocols. These frameworks and policies would help the organisation to be prepared and guide the escalation process for such issues so as to minimise losses in both financial and non-financial aspects. More importantly, Directors need to set a strong tone from the top that such acts are not tolerated and lead by example.

### Understanding an activist's agenda

Activists are looking for opportunities to disrupt, and are challenging Boards and executives across all areas of governance, strategy, operations and sustainability, all in the name of maximising shareholder value.

Even companies in the United States, where activism has been more commonplace, are not well prepared. In general, they react to the concerns of a vocal group of shareholders or the targeted campaign of an activist/activist group. Companies in Singapore stand to gain strategically, by adequately preparing both to pre-empt activism and prepare for an activist threat before it happens.

A recent roundtable held by KPMG US of 1,200 directors from across 25 cities, illustrated that only 18% of respondents had performed social media vulnerability assessments. These assessments offer Boards an independent understanding of the risks and opportunities facing their companies and position them to address the risks and challenge management to improve long term performance, before an activist comes knocking.<sup>254</sup>

254 KPMG LLP, Rethinking Shareholder Engagement in the Age of Activism (<http://www.kpmg-institutes.com/content/dam/kpmg/auditcommitteeinstitute/pdf/2014/Rethinking%20Shareholder%20Engagement%20in%20the%20Age%20of%20Activism.pdf>)



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
- ▶ 18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

Another study conducted by MyPaper (2011) also found similar results that out of 4,000 respondents poll in 12 countries and territories, 63 per cent stated that social media was a serious security risk, but only 29 per cent reported having the necessary controls in place.<sup>255</sup>

In order to be truly strategic, Boards and management should understand the issues that currently attract activists and be forward looking to the issues of the future, while building strong relationships with stakeholders. Stakeholder engagement is a critical part of the solution and is discussed in more detail in [Chapter 13](#).

### Managing social media risks within the organisation

Increasing stakeholder activism, particularly through social media, poses multiple risks to the company and puts the Board, management and the company's public relations capabilities in the spotlight. Management must consider arming itself with a plan for responding to an 'attack'. The plan should include details for the establishment of a response team that could assist in understanding the activists concerns, and by evaluating any proposed responses, to ensure reactions are well thought through and not emotional.

It is the responsibility of the Board to ensure that the strategy considers the range of risks that social media poses – be it the specific issues that can be raised (with speed and scale) through social media channels (the external risks), or the issues associated with how social media is managed within the organisation (the internal risks).

<sup>255</sup> MyPaper. (2011, October 14). Growing use of social media puts firms at risk. Retrieved from <http://www.stjobs.sg/career-resources/workplace-success/growing-use-of-social-media-puts-firms-at-risk/a/27627>

Examples of such mitigation of internal risks would be cases at major banks such as Deutsche Bank, J.P. Morgan and RBS banning the use of mobiles on trading floor, chat platforms and enforcing stronger compliance team to enhance communication guidance and surveillance. The Association of Banks in Singapore also revised its Code of Advertising Practice for Banks in 2010 and Monetary Authority of Singapore (MAS) introducing its Technology Risk Management Guidelines to regulate the use of technology specifically for financial services, and such technology expressly included the use of the internet and social media platforms.<sup>256</sup>

The Board must also ensure that the social media strategy is effectively implemented by management and that clear protocols are established that outline the key roles and responsibilities of the Board, individual directors and management when responding to any social media crisis in the public forum.

When reviewing the organisation's social media strategy, the Board should look for what risks are identified and how the strategy is aligned to the broader stakeholder engagement framework. The social media strategy should establish a framework that provides for a high degree of coordination between Corporate Communications, Investor Relations, management and the Board, and is supported by monitoring and escalation procedures.

The key to social media is to turn the risks into opportunities. Without a strategy, a company may see social media as a minefield to navigate, knowing well that timing with social media is everything, where statements and comments are almost impossible to fully retract, and

<sup>256</sup> Gye, H. (2015, August 15). Panicking banks ban mobile phones, swearing and even emojis in bid to avoid repeat of Libor humiliation - but new rules could drive traders away because they 'stop the job being fun'. Dailymail. Retrieved from <http://www.dailymail.co.uk/news/article-3194053/How-banks-banned-phones-swearing-emojis-Libor-scandal.html>

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
- ▶ 18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

where they will be subject to scrutiny with one wrong being potentially heavily criticised.

Due to the contemporary nature of social media, many of the risks are difficult to quantify and, as a result, many of the risks or enablers of those risks go undetected. It is for this reason that a comprehensive, logical and practical approach is needed to identify and mitigate the risks. In many respects this approach should mirror traditional best practice risk management frameworks which involve an assessment of potential scenarios and consideration of their probability and impact. For example, what is the impact on our operations if one of our suppliers is identified through social media as having contravened our policies and contractor arrangement?

There are practical tools and frameworks that can be applied in order to appropriately manage social media risks. These tools consider the external landscape, internal controls and policies. A key element of managing social media risks is to first identify the possible exposures and gaps through a regular 'diagnostic' or review. Leading organisations are embedding these diagnostic reviews into the internal and external audit process.

The key to an effective social media risk mitigation strategy is:

- explore social media conversations that not only mention the organisation, but also include broader industry issues, suppliers and emerging organisational concerns
- consider the internal processes and controls in place to deal with a social media risk, as well as in the event of an adverse event caused by or playing out on social media
- develop the necessary governance framework to address any identified gaps after the review and on a rolling basis turning those governance frameworks into workable processes and procedures.

## Key success factors

Best practice in this space is awarded to organisations that act early to absorb the concerns on social media, and establish a credible narrative about the organisation's response to growing discontent. Organisations that have a dedicated social media intelligence monitoring program, that comprises both of data and experienced strategic counsel, will be best placed to know when and how to respond.

Stakeholders' appetite for social media has not been equally matched by companies, providing companies with an opportunity to improve and increase their social media engagement with stakeholders.

Companies should be leveraging social media to engage 'real time' with stakeholders, by instantly communicating with, and educating stakeholders on the company's strategy and how it is maximising shareholder value. A proactive social media risk strategy is critical. A good example of this recognition is the active involvement on social media by the Prime Minister Lee Hsien Loong and other members of Parliament to connect with Singaporeans (66 per cent of the population use social media – We Are Social statistic).<sup>257</sup>

## Role of the Board

Boards need to take an active role in ensuring social media risk is effectively addressed. Managing and mitigating social media risk is not solely reliant on technology and, therefore, the Board needs to support a social media 'risk-aware' culture.

<sup>257</sup> Soon, C. (2015, June 19). Social media's influence in Singapore politics here to stay. IPSCommons. Retrieved from <http://www.ipscommons.sg/social-medias-influence-in-singapore-politics-here-to-stay/>

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
- ▶ 18. Social media
19. Investment committees
20. Workplace safety & health
21. Appendices

Directors should be raising this as a discussion item at Board meetings by taking a fresh look at stakeholder engagement, the company's social media strategy and the use of vulnerability assessments as a better practice strategy for being prepared for the coming rise in Singapore stakeholder activism.

The Board should:

- Ensure that the organisation is making the best use of social media through ongoing management reporting of company competitor and market intelligence
- Ensure that a social media risk management strategy is in place and that there are effective oversight mechanisms established to monitor and manage the key risks identified
- Ensure that a vulnerability assessment is undertaken periodically to identify possible 'target' areas of stakeholder activism. This should inform the social media risk strategy
- Require management to continuously monitor/scan the social landscape to enable effective challenge of the risks and opportunities within management's social media strategy
- Know and remain engaged with your stakeholders.
- Encourage thinking around the disruption or potential impact of emerging digital technologies on your industry
- Request 'Social Media Intelligence and Risk Reports' as part of their Board papers. This provides a ground level view of how the organisation is perceived and the direct line of sight to emerging risks

- Challenge the perception that marketing is adequately managing social media risk
- Encourage social media to be grouped in with other more traditional risks
- Take steps to require management to actively investigate the use of social media platforms like Twitter, LinkedIn and Facebook by the organisation
- Undertake training to understand the impact of social media and how the various platforms work.

### Useful references

- Stanford Graduate School of Business, Monitoring risks before they go viral: Is it time for the Board to embrace social media?, 5 April 2012, <http://www.gsb.stanford.edu/sites/default/files/research/documents/CGRP25%20-%20Social%20Media.pdf>
- KPMG, Social media risk management: why it matters and what you need to know, 2014, <https://home.kpmg.com/au/en/home/insights/2015/06/managing-risks-social-media.html>
- KPMG LLP, Rethinking Shareholder Engagement in the Age of Activism <http://www.kpmg-institutes.com/institutes/aci/articles/2014/07/rethinking-shareholder-engagement-in-the-age-of-activism.html>

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
- ▶ 19. Investment committees
20. Workplace safety & health
21. Appendices

# 19. Investment Committees

Investment committees are charged with overseeing corporate investments and developing investment policies for Board approval such as to invest funds to meet both short and long term obligations.

## Questions that company Directors should ask

- |  |   |
|--|---|
| 1. Are directors convinced that their and management's risk appetites are aligned for each investment/financial risk?            | 6. Would it be useful to employ an external specialist advisor utilised for advice on asset allocation strategies?  |
| 2. Does the Investment Policy make sense intuitively, including articulating the rationale for a particular investment strategy? | 7. Is there separation of duties between the custodian, fund manager and asset consultant (e.g. it is preferable for the asset consultant not to be providing investment products)? |
| 3. Do the investment mandates given to service providers, such as fund managers, align to the Investment Policy?                 | 8. Is investment management performance regularly reviewed and critically examined?   |
| 4. Is there a process to monitor compliance with the Investment Policy – including by outsourced service providers?              | 9. Is investment management performance exceeding index-based performance – because if it is not – then why is the organisation paying additional fees for 'active management'?     |
| 5. Is the investment selection process documented and undertaken by appropriately qualified investment management staff?         | 10. Are investment management fees and custodian fees regularly reviewed and periodically tested to market?   |

## Red flags

- |  |  |
|--|--|
| ▶ Lack of a formal, documented and comprehensible Investment Policy. It should be easily understood by a competent, but non-technical Director | ▶ There is a lack of independent verification of performance or compliance with the Investment Policy  |
| ▶ An investment performance benchmark is either deemed not appropriate or is not established   | ▶ Non-compliance with Investment Policy – which may be consistent in nature or not be detected in a timely manner                                      |
| ▶ The performance of external managers is not measured or reviewed   | ▶ Management is very defensive when asked logical questions or becomes aggressive towards third parties, such as auditors, when reasonably challenged  |
| ▶ There appears to be inadequate segregation of duties, inadequate controls and breach reporting is either not formalised or is inadequate     | ▶ There is a high dependence on one key individual in terms of the management of funds   |
| ▶ There are large variances in reported performance over periods   | ▶ There is confusion at the Investment Committee in terms of interpreting various reports or advice received from parties, such as an asset consultant |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
- ▶ 19. Investment committees
20. Workplace safety & health
21. Appendices

In a study of 545 listed companies, only 4.4% of companies (24 in total) indicated that they had formed an Investment Committee<sup>258</sup>. However, while this percentage is small, it should not be mistaken that investment activities are restricted to only certain entities such as asset and wealth managers (investment managers and banks), insurers, and health funds. In fact, any organisation can establish an Investment Committee, which has the task of prudently investing funds whilst balancing the need to obtain a reasonable return with managing the portfolio so that it operates within the agreed risk appetite and tolerance.

This must be achieved within a robust risk and reporting framework to achieve compliance with applicable regulatory requirements.

This section of the Director's Toolkit provides guidance to Directors who are responsible for overseeing investment governance, operations and processes. Due to the need for brevity, as well as the complexity of various regulatory environments, this section covers the general issues associated with better practice investment governance, rather than specific regulatory requirements. Further references that go into more detail are provided at the end of this chapter.

### Board's role

Ultimately the Board is responsible for investment management including the overall investment beliefs and philosophy, the investment strategy, Investment Policy and associated risk appetite and tolerance.

Even though the Board may delegate these responsibilities, either in total or in part, to a Board committee, such as the Investment Committee, or rely

on the advice of an asset consultant, the Board is still ultimately responsible for investment management.

### Investment committee

The Investment Committee traditionally tends to be a Board committee, rather than a management committee, and is responsible for the investment strategy as delegated by the Board. The Investment Committee would also be responsible for the monitoring of investment performance and either approving investment decisions or recommending investment strategies to the Board in line with its charter and delegations.

The Investment Committee should comprise of at least three directors, the majority of whom are independent. It is also appropriate for directors in the Investment Committee to hold positions in the Board Risk Committee, as investment policies must be within the company's risk appetite and aligned with its strategic framework. However, membership of the Audit Committee and Investment Committee should be mutually exclusive, so as to preserve the independence of the Audit Committee. In this context, companies which have an integrated Audit and Risk Committee should not have common members with the Investment Committee.

Further details regarding Board committee composition and structures are provided in [Chapter 9 Board committees](#).

### Investment framework

The investment framework supports the organisation's process for formulating an investment strategy. An investment framework includes the governance, policies, systems, processes and people to operate and oversee the management of investments, including the management of the investment and financial risks.

258 SGX-KPMG CG Disclosure Study 2016



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
- ▶ 19. Investment committees
20. Workplace safety & health
21. Appendices

### Risk appetite

The collective risk appetite of the organisation is a key determinant in the construction of the investment portfolio. It is important that the risk appetite of the Board and management are aligned (which is often not the case) and, ultimately, it is the Board's risk appetite which is paramount.

Risk appetite is driven by a number of factors, including:

- The amount of funds available for investment (i.e. the greater the amount the more diverse and sophisticated the investment choices)
- The period of time over which funds are available (i.e. generally, short-term equates to a lower risk, longer term enables greater risk. Exceptions to this include long-term bank deposits where the longer term risk is generally low)
- The ability to withstand volatility in the investment portfolio (i.e. less than one in X years chance of negative returns)
- Capital requirements (i.e. for insurance companies, higher risk investments require higher levels of capital)
- The complexity of investments
- The capability and experience of the investment framework, including personnel
- The requirement to make regular dividends/distributions to share/unit holders
- Restrictions on certain types of asset class, based on the ethical, social or environmental risks (e.g. the tobacco industry)
- Investment diversity guidelines for the portfolio, including minimum credit ratings of investment managers

- The values of the organisation and the types of investments it is, and is not, willing to make.

Once the 'risk appetite' has been agreed then the investment selection/asset allocation process can commence.

### Risk tolerance

Risk tolerance sits hand in glove with the risk appetite of the organisation. Risk appetite focuses on defining the boundaries within which investments are made. It is a higher-level statement that defines the amount of risk the organisation is willing to take in order to meet its investment objectives. Risk tolerance is the degree of volatility that the organisation is willing to accept within the parameters of its risk appetite.

For example, an organisation's risk appetite statement may state that it does not accept risks that could result in a 'significant loss in revenue'. A risk tolerance statement would then go on to define the specific levels of acceptable variation within that risk (e.g. the organisation may only accept a 10% loss in revenue from a particular asset class in any given period).

The questions to consider in the development of the organisation's risk tolerance statement are therefore inherently linked to those used to develop the risk appetite.

### Investment strategy

The investment strategy is the key document defining the strategic investment objectives and the guiding framework and principles determined by the Board to be appropriate for the organisation's broader operating strategy. Its key components may include:

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
- ▶ 19. Investment committees
20. Workplace safety & health
21. Appendices

- Asset allocation principles – such as how the portfolio will be constructed in order to meet the desired risk/return outcome
- Risk management guidelines – including clear risk appetite and risk tolerance
- High-level policy statements, including the monitoring framework that details what will be monitored and the specific measures in place to track performance
- Investment purpose and the alignment of organisational values to the investment strategy (e.g. 'ethical' investment principles).

### Asset allocation

To implement the investment strategy, the organisation should have an asset allocation process in place which includes robust due diligence. Asset allocation involves dividing an investment portfolio among different asset categories/classes. This is a crucial step to ensure that investments selected are aligned to the organisation's investment objectives, including risk appetite and tolerance.

The due diligence process should consider historical returns for particular asset classes and the volatility of return/value of the instrument (i.e. risk) over various time periods. Considering these factors can be insightful and assist in identifying correlations between assets, while helping to dispel common preconceptions about various assets. For example, some assets may be considered to have low returns, but when looked at over the long term, they perform well with low volatility, providing a form of capital protection.

Another relevant example in asset allocation is where funds are needed in the short term and a loss cannot be tolerated. Therefore, the logical asset allocation would be to defensive assets such as cash, term deposits and short

dated fixed interest securities, which impacts the return that can be achieved.

Many research and academic articles indicate that asset allocation is a key driver of returns, rather than stock or security selection – hence the importance of having a robust framework and process to determine asset allocation.

Having allocated assets, an organisation should also have arrangements in place for the ongoing management and monitoring of its investment strategy. Depending upon the value of funds invested, this may include asset allocation rebalancing processes, exposure management arrangements (i.e. derivatives and currency), investment transition arrangements, processes to monitor investments and valuation procedures. It is critical that the reporting framework to monitor investments provides directors with meaningful information in a timely manner.

### Financial risk management

When directors are overseeing the investment process, they need to be mindful of the financial risks associated with the investment process and not just the asset allocation decision.

A robust risk management framework needs to be established and implemented to address the risks arising from the investment of funds. These risks would include:

- Liquidity risk (ensuring that investments can be readily converted to cash, if required, without suffering a significant loss or that sufficient cash is held as part of the investment portfolio)
- Credit risk (the risk of loss resulting from counterparty default)
- Market risk (the risk of loss in value of investments)

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
- ▶ 19. Investment committees
20. Workplace safety & health
21. Appendices

due to the adverse effects of movements in interest rates, equity prices, foreign exchange rates, commodity prices, etc.)

- Operational risk (the risk of loss resulting from errors in the processing of transactions, a breakdown in the control environment or errors or failures in systems)
- Reputational risk (the risk of damage to the reputation of the organisation due to the nature of the investment or loss in value of the investment – particularly important for Government and widely owned organisations)
- Social and environmental risk (the risk associated with failing to meet ethical, social and environmental expectations that generate a loss of business value through stakeholder activism and perceptions of the organisation's misalignment of its business to the broader societal values).

Financial risk management arrangements would typically comprise a range of tools for risk measurement and analysis that are commensurate with the investments of the organisation. One very good example of this is the use of stress testing and scenario analysis, which can assist the organisation to identify and assess potential risk exposures that may threaten the likelihood of achieving investment objectives. Stress testing should be a forward-looking assessment of possible risk factors. Importantly, the outputs from stress testing should enable directors to make informed decisions on the management of the portfolio to enhance returns and reduce financial risk.

### Investment Policy

Having determined the investment beliefs and philosophy, objectives, strategy, risk appetite, risk tolerance and approach to financial risk management, it is important that this is documented in the Investment Policy.

The fundamental importance of an Investment Policy is that it provides the framework for an organisation to achieve its investment objectives (as defined in the investment strategy) and seeks to avoid unacceptable outcomes. The policy ensures that the risk appetite and philosophy of the organisation are reflected in its investment activities.

The purpose of the policy is to provide general guidance regarding the investment objectives, specific guidance on strategies to achieve the investment objectives, and to provide a mechanism to control management behaviour and reduce bias and potential errors arising from decision making. The Investment Policy and procedure should address the key areas of and include:

- the investment objectives, philosophy, risk appetite and risk tolerance, including an explicit mandate for values-led/ethical investment strategies (e.g. not investing in gaming, tobacco)
- the asset allocation strategy and the rationale by which those objectives are to be pursued
- guidelines on investment exposures and maturity periods
- the mandates with which underlying investments must comply and, in the case of pooled investments, the mandates with which the managers must comply
- any socially responsible investments and prohibited investments
- the benchmarks against which the performance of investments and managers are to be assessed
- the valuation approach and methodology for unlisted or illiquid investments
- the methodology for deciding and disclosing proxy voting decisions

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
- ▶ 19. Investment committees
20. Workplace safety & health
21. Appendices

- the reporting required to be provided to the Investment Committee and the Board
- the responsibilities of various stakeholders, including the Board, Investment Committee and management.

### Example – Controlling the use of investment funds

Generally, investment agreements and subscription of capital agreements allow investors to define how their invested capital is to be utilised by the target company. This can be done through a 'Manner of Use' clause. Alternatively a 'Manner of Use' document would serve a similar purpose, by requiring the target company to state how it will use the investment monies<sup>259</sup>.

In 2012, Tembusu Growth Fund Ltd invested S\$1.5 million in Acatek, Inc. with the purpose of keeping the Actatek group "functioning as a going concern, to facilitate expansion and restructuring of the group and to ensure that it had sufficient funds to achieve listing". The agreement contained a Clause which required Acatek to deliver a Manner of Use Document, detailing how it will use the proceeds of the investment and an execution plan for its expansion. While the document stated that the investment would be used generally in "Sales and marketing expenses, R&D expenditure, IPO, and Working Capital", Acatek used some of the investment monies to repay monies owing to its directors. Thus in the decision of the High Court, it was found that the Manner of Use Document was not just descriptive but rather prescriptive and Acatek was bound to use the investment monies in accordance with it.

<sup>259</sup> Sunil Rai; Controlling the use of investment funds: Tembusu Growth Fund Ltd v Acatek, Inc. Retrieved from: <http://www.lexology.com/library/detail.aspx?g=8864e6ae-9306-46a2-9366-e338f78b9537>

This case emphasises the importance of ensuring that the Manner of Use clause or document are recognised as integral to the investment agreement. Proper integration will prevent the company from using the investment monies for purposes outside the investor's intention.

This is particularly important when the Investment Committee invests in private equity such as venture capitals and may not be able to actively monitor the use of its funds by the company and its management.

### Investment performance and risk management reporting

Having executed the investment strategy, the investment performance and risk management reporting will need to be undertaken to measure the performance of investment activities against the investment objectives and benchmarks. At a detailed level, this will involve comparing the performance of investments and managers to agreed benchmark indices. Other considerations include:

- Frequency (usually a minimum of monthly reporting)
- Documentation – the reporting process should be documented in procedures
- Detail/content (e.g. manager performance, compliance, portfolio values, credit risk and other risks)
- Format, such as the use of an 'Investment Report Dashboard'
- Distribution (i.e. Executive Management, Middle Office/ Compliance function Investment Committee etc.).

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
- ▶ 19. Investment committees
20. Workplace safety & health
21. Appendices

### Outsourcing – Fund managers and external providers

Depending upon the size of the funds available for investment, the outsourcing of various activities may be appropriate. This could include the outsourcing of investment activity to fund managers, the use of asset consultants to determine asset allocation and the use of a custodian for the settlement and recording of investment transactions. However, there is also a risk arising from the outsourcing of activities which needs to be recognised and managed.

Outsourcing and the use of external providers should also take into account:

- The benefits of outsourced investment management given the capabilities of in-house staff and the complexity of investments
- The nature of asset classes invested in
- The scale and size of investments
- System requirements to support outsourced arrangements
- The use of index funds versus active investment manager funds
- External manager assessment, selection and monitoring processes
- The custody and investment administration requirements.

It is also important that the 'mandates' given to investment service providers, particularly fund managers, are consistent with the Investment Policy. It is not uncommon for an Investment Policy to prohibit the use of derivatives, only to find a fund manager using derivatives – because it is not prohibited in the mandate provided to the fund manager.

Critically, an organisation can outsource its investment activities, however, it cannot outsource its legal accountabilities and responsibilities. Directors and Investment Committee members should also consider the MAS Guidelines on Outsourcing for prudent risk management practices in relation to outsourcing<sup>260</sup>.

### Useful references

Certain industries such as Banking and Insurance are subject to various regulatory requirements by MAS relating to the management of investment funds. It should also be noted that activities pertaining to Securities, Futures and Funds Management are governed under the Securities and Futures Act (SFA)<sup>261</sup>.

260 Chapter 289, Securities and Futures Act:  
<http://statutes.agc.gov.sg/aol/search/display/view.w3p;page=0;query=DocId%3A25de2ec3-ac8e-44bf-9c88-927bf7eca056%20Depth%3A0%20Status%3Ainforce;rec=0;whole=yes>  
 261 <http://www.mas.gov.sg/-/media/MAS/Regulations%20and%20Financial%20Stability/Regulatory%20and%20Supervisory%20Framework/Risk%20Management/Outsourcing20Guidelines.pdf>



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
- ▶ 20. Workplace safety & health
21. Appendices

# 20. Workplace safety & health

Every workplace is exposed to health and safety risks, no matter what industry they operate in. Employers are also responsible for the health and safety of all workers. Setting a well-designed strategy leads not only to an engaged workforce, but a productive one too. Health and safety is fundamental for all organisations and begins with the Board.

## Questions that company Directors should ask

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|--|--|
| 1. Does the Board have oversight of a clear health and safety strategy with performance indicators and targets? Are these targets realistic?                     | 6. Is there a culture that values and prioritises health and safety within the organisation?   |
| 2. How does the Board hold management accountable for implementing health and safety strategy and policy and ensure that the CEO meets the Board's expectations? | 7. What audits or assessments are undertaken to provide assurance over health and safety management processes?                         |
| 3. How does the Board demonstrate its commitment to a positive health and safety culture?  | 8. How does the Board ensure it is satisfied that it has obtained competent health and safety advice from management or other parties? |
| 4. Does the Board understand the legal and health and safety framework in which they operate?  | 9. What information does the Board receive about health and safety performance to make informed decisions?                             |
| 5. Has the Board received the appropriate training to enable it to challenge health and safety management?   |  |

## Red flags

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|--|--|
| ▶ There are no Board level objectives and targets for health and safety  | ▶ Where there has been significant organisational change, the implications for health and safety have not been reported to the Board   |
| ▶ There is no Board oversight of the organisation's health and safety strategy   | ▶ Contradictory/counter performance indicators (e.g. workers compensation claims costs, frequency and duration are escalating, yet other safety key performance indicators, such as lost time injury frequency rates, are improving) |
| ▶ Health and safety information does not appear on the agenda for Board meetings   | ▶ Material health and safety risks are ignored or undisclosed (e.g. contractor performance is ignored, where contractors contribute to the workforce, or where the company has overseas operations)                                  |
| ▶ Board members have not received appropriate information and training on their health and safety responsibilities   | ▶ Health and safety risks are not considered within the organisation's risk management framework   |
| ▶ Board reporting of health and safety performance is based only on lagged indicators (e.g. number of incidents) rather than leading indicators (e.g. number of safety audits or training) |  |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
- ▶ 20. Workplace safety & health
21. Appendices

### Key concepts – Health and safety

Organisations have a duty of care to ensure that any person affected by the company's undertakings remains safe at all times and their work activities are not prejudicial to health.

Having a strong health and safety culture, and an embedded, effective health and safety management system by which managers and workers demonstrate accountability, can result in significant benefits for an organisation. The failure of organisations to effectively manage health and safety risks and performance has both human and business costs and, as such, should receive the same priority by directors as all other risks.

Health and safety governance is as important as any other aspect of governance and is core to an organisation's overall risk management function and a key responsibility of directors.

### Legislation

All directors have a legal imperative to ensure that the organisation which they represent remains compliant with relevant health and safety legislation.

In Singapore, the Workplace Safety and Health ("WSH") Act focuses on the duties and liabilities of:

1. Employers – a person who, in the course of the person's trade, business, profession or undertaking, employs any person to do any work under a contract of service
2. Principals – 'contractor' means a person engaged by another person (referred to in this Act as the principal) otherwise than under a contract of service —
  - (a) to supply any labour for gain or reward; or
  - (b) to do any work for gain or reward,

in connection with any trade, business, profession or undertaking carried on by the principal.

The Act does not specifically confer duties upon directors. Nonetheless, directors still have certain responsibilities in the capacity of a WSH officer.

### Strategy

It is the duty of the Board to ensure the organisation has the right strategic direction for health and safety, which is underpinned by robust systems, processes and people. Ultimately, Boards are responsible for determining the organisation's high-level health and safety strategy and policy, which managers are required to implement. This strategy and policy should also include consideration of all persons impacted by the organisation's activities, not just employees (e.g. contractors and visitors). However, Board responsibility should go beyond the issuing of strategy and policy, to also ensure that the implementation of the health and safety policy is effective, by holding management to account through processes of policy and planning, delivery, monitoring and review.

With an aging workforce, the impact of chronic disease in the workplace and a competitive labour market, businesses using targeted strategies to build health and well-being at work will have greater business performance and people outcomes. In addition, measuring health and safety performance provides an insight into management and investment decisions.

As part of the strategic direction, directors should consider and challenge the key performance indicators that the company strategy is linked to. For example, safety performance (particularly numbers of/nature of incidents) is often reported by management, yet there is little/no disclosure on the impacts on health (mental and physical wellness), which often have a much greater impact on a business.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
- 20. Workplace safety & health
21. Appendices

### Governance

#### *Director competence*

All directors should have a clear understanding of the key health and safety issues for their organisation and be continually developing their skills, knowledge and understanding in this area.

#### *Director roles and responsibilities*

All directors should understand their legal responsibilities and their role in governing health and safety matters for their organisation. Their roles should be supported by formal individual terms of reference, covering, at a minimum, the oversight of health and safety strategy development, policy, setting standards, performance monitoring and oversight of an internal controls framework. Emerging practice is to have a committee of the Board with the role of overseeing and challenging the health and safety governance process (See Chapter 9 – Board Committee).

#### *Culture, standards and values*

The Board should take ownership for key health and safety issues and be ambassadors for good health and safety performance within the organisation, upholding core values and standards. They should set the tone at the top, and establish an open culture across the organisation with a high level of communication on health and safety issues.

#### *Strategic implications*

The Board is responsible for driving the health and safety agenda. They have oversight and an understanding of the risks and opportunities associated with health and safety, including any market pressures which might compromise the values and standards – ultimately establishing a strategy to respond.

### *Performance management*

The Board should ensure they retain oversight of the key objectives and targets for health and safety management, and create an incentive structure for senior executives which drives good health and safety performance, balancing both leading and lagging indicators, and capturing both tangible and intangible factors. Non-executives (through the Remuneration Committee, where one exists) should be involved in establishing the appropriate incentive schemes.

### *Internal controls*

The Board should ensure health and safety risks are managed and controlled adequately and that a framework to ensure compliance with the core standards is established. It is important that governance structures enable management systems, actions and levels of performance to be challenged. This process should utilise, where possible, existing internal control and audit structures and be reviewed by the Audit Committee, or other suitable committee or Board members, where necessary.

The Board may establish a separate Board Risk Committee or otherwise assess appropriate means to assist it in the carrying out of its responsibility of overseeing the company's risk management framework policies<sup>262</sup>. Such a committee may be established to address WSH, especially in high risk industries such as construction, oil and gas, and health, where staff are placed in complex production or service environments.

262 Singapore Code of Corporate Governance 2012

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
- ▶ 20. Workplace safety & health
21. Appendices

### Organisational structures

The Board should integrate health and safety governance processes into the main corporate governance structures within the organisation, including the activities of the main Board and its committees, including risk, remuneration and audit. In some cases, the creation of an additional Board committee to consider health and safety (and/or risk/corporate responsibility) matters may be relevant.

### Due diligence

Regardless of the size of the undertaking or the nature of the organisation's health and safety risk profile, it is important that directors, as officers, are fully informed of the relevant health and safety matters and requirements that apply to them. This includes understanding their role in governing health and safety, as part of their broader responsibilities of good corporate governance.

The exercise of due diligence is the individual obligation of each officer of the body corporate. This means that each individual officer should consider how they will demonstrate their due diligence requirements in compliance with the WSH Act.

### How do directors/officers demonstrate due diligence?

It may be noted that the duty to exercise due diligence is contained within a director's duty of care and skill. Further details regarding Directors' Legal Duties provided in [Chapter 1](#).

Some of the examples where the duty of care and skill may not be satisfied:

- Attending Board meetings without reading papers

- Failing to make further enquiries/seek more information when in doubt about certain matters such as:
  - Company is venturing into new business sector and only cursory information about the new business is provided
  - Knowing potential safety and health breaches
  - New laws are being introduced and not checking to see how they could impact the company.

In Singapore, the Workplace Safety and Health (WSH) Institute has developed a National WSH Leadership Framework to strengthen the competencies of business leaders to create safe and healthy workplaces in Singapore. The desired outcomes for individual business leaders and directors, as well as for the companies, are listed above<sup>263</sup>.

### Case Study – Offences by bodies corporate and Directors' Liabilities

In March 2010, Kay Lim Construction & Trading entered into a rental agreement with Soon Douglas Pte Ltd for the dismantling and removal of tower cranes at a project worksite. Unknown to Kay Lim, Soon Douglas had subcontracted the dismantling and removal of the tower cranes to Chit Guan Engineering Resources. In the dismantling and removal works, a tower crane collapsed whilst it was being jacked down. One employee was killed and three others were injured. It was found that Chit Guan's team of workers failed to adhere to the safe method of dismantling and jacking down of the tower crane.

Following investigations into the accident by the Ministry of Manpower (MOM), the Director of Chit Guan pleaded

<sup>263</sup> <https://www.wsh-institute.sg/files/wshi/upload/cms/file/Leadership%20in%20WSH.pdf>

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
- ▶ 20. Workplace safety & health
21. Appendices

guilty under the WHS Act<sup>264</sup> to not having 'exercised all such diligence to prevent the commission of the offence as he ought to have exercised having regard to the nature of his functions in that capacity and to all the circumstances.' He was fined \$15,000 and the supervisor of the site was imprisoned for one month.

The case showed that directors have a clear legal duty to exercise due diligence to ensure that the organisation's day-to-day activities do not contravene any sections of the WHS Act or could be legally held responsible for the lapses in WSH.

### Penalties

In Singapore, penalties apply to any person guilty of an offence under the WHS Act. Specific penalties are provided in specific sections and apply only to certain contraventions. However, where specific penalties are not provided, the general penalties pursuant to s50 of the WHS Act are:

|                       |   |
|-----------------------|---|
| <b>Natural person</b> | Fine not exceeding \$200,000 or to imprisonment for a term not exceeding 2 years or to both |
| <b>Body corporate</b> | Fine not exceeding \$500,000  |

Stiffer penalties are provided for in s51 of the WHS Act for repeat offenders (at least one previous occasion been convicted of an offence under this Act), and offences that have resulted in death. It should also be noted that contravention that continues after conviction warrants a further offence and fine.

264 <http://www.singaporelaw.sg/slaw/laws-of-singapore/case-law/free-law/high-court-judgments/14987-kay-lim-construction-amp-trading-pte-ltd-v-soon-douglas-pte-ltd-and-another-2012-sghc-186>

Apart from the penalties imposed for such offences, the Commissioner has the power to issue a stop-work order in certain circumstances, which will also serve as a preventative measure for any potential breach in WSH.

### Moving forward

The number of workplace death incidents in Singapore increased in 2015 (66, up from 60 in 2014<sup>265</sup>). With another increase in early 2016 of 6 deaths relative to the same period in 2015, the MOM have imposed a stricter punishment regime. On 12 May 2016, Ministry of Manpower ("MOM") raised the minimum time for companies ordered to stop work from two to three weeks to resolve the issues, and would be unable to employ new foreign workers until the safety issues have been remediated.<sup>266</sup> These measures by MOM will ultimately affect the bottom-line of companies as well as potential reputational losses due to delays in deadlines.

Directors need to be aware of the risk that contractors and employees may be under significant pressure from management and may resort to cutting corners, through breaching safety requirements or protocols, to meet their deadlines. Under the due diligence provisions of the WHS, failure to be aware of these breaches will not be a valid defence.

### Performance management

'Man-days lost' or 'downtime' have become the cornerstone of mainstream injury/incident reporting in Singapore and the benchmark against which organisational, industry and national comparisons are made. Although downtime is being measured to inform an ever growing range of health and safety problems

265 OSHD Annual Report 2015

266 Ho, O. (2016, May 25). Concern over rising workplace deaths. Straits Times. Retrieved from <http://www.straitstimes.com/singapore/manpower/concern-over-rising-workplace-deaths>



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
- 20. Workplace safety & health
21. Appendices

and decisions, they also have a number of important limitations, such as a poor correlation with both the human and financial consequences of work related injury and illness<sup>267</sup>. There are also considerable variations in the definition of 'lost time' across organisations, thereby making performance benchmarking comparisons difficult.

'Lagging' indicators such as number of man-days lost, however, may not provide sufficient information for successful management nor provide appropriate information for due diligence purposes. For example, lagging indicators may provide information too late for management to respond.

The Board should periodically monitor the performance of the organisation with respect to WSH issues. Key performance indicators should be established and reviewed for such purposes. More specifically, 'leading performance indicators' ("LPIs"), can be used. Because LPIs provide valuable information that help the user respond to changing circumstances and take action to achieve desired outcomes or avoid unwanted circumstances, they can play an important role in motivating continuous improvement, with a focus on areas that have the potential to cause an incident, before the incident itself is realised – which is of the utmost importance in the domain of WSH.

### What health and safety information should be provided to the Board?

Directors should ensure the appropriate level of information is being reported by management to the Board.

These reports should be inclusive of lead and lag indicators, and have sufficient information to support the Board's decision making. This should be supported by independent and objective assurance – thus bringing a systematic, disciplined approach to health and safety risk management, control and governance processes.

For leading performance indicators to be successful, they need to be selected carefully, for example, targeting the material issues and setting sufficiently challenging targets. Setting a leading performance indicator and getting a good score does not automatically improve performance. It is not the numbers that are important, but the quality and application of the gathered information that makes the difference.

### Useful references

- Link to the legislation and related acts - <http://www.mom.gov.sg/legislation/workplace-safety-and-health> -
- Useful summary of: what the act covers; responsibilities; penalties; hazardous substances and machinery and equipment. <http://www.mom.gov.sg/workplace-safety-and-health/workplace-safety-and-health-act> -
- Workplace Safety and Health Council – offers guidance and training on implementing acceptable WHS practices. <https://www.wshc.sg/> -
- Workplace Safety and Health Institute – an initiative to build the WSH practices of Singapore to be leading practice by 2018. <https://www.wsh-institute.sg/>

<sup>267</sup> Issues in the Measurement and Reporting of Work Health and Safety: A Review, Safe Work Australia, November 2013.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
- 21. Appendices

# 21. Appendices

## Appendix 1: Example Board charter

The purpose of a Board charter is to describe the Board's terms of reference and outline the Board's approach to important governance practices including corporate sustainability.

### Board Charter

Adopted on [date of adoption]

### 3. Overview

The Board is primarily responsible for ensuring that [name of company] (the "Company") has an appropriate corporate governance structure aimed at creating and protecting shareholder value including consideration of financial and non-financial material factors. This Charter explains the Company's commitment to corporate governance and sustainability.

### 4. Roles and Responsibilities Board

The principle role of the Board is to set the Company's vision and to regularly review its strategic direction. The Board has the responsibility for corporate governance and sustainability and oversees management's control and accountability framework. The Board is ultimately accountable to the Company's shareholders for the performance of the business and the integration of sustainability issues as part of its strategic formulation.

### Chairman

The Chairman is to be an independent non-executive director. He or she is responsible for:

- a) Leadership of the Board;
- b) Overseeing the Board in the effective discharge of its supervisory role;
- c) The efficient organisation and conduct of the Board's functions and meetings;
- d) Facilitating the effective contribution of all directors;
- e) Briefing of all directors in relation to issues arising at meetings;
- f) The promotion of constructive and respectful relations between Board members and the Board and management;
- g) Committing the time necessary to discharge effectively his or her role as Chairman; and
- h) Scheduling regular and effective evaluations of the Board's performance.

### Chief Executive Officer (CEO)

The CEO is responsible for the executive management of the Company, and is accountable to the Board for the day to day operations. The CEO is authorised to delegate such powers conferred on him as he deems appropriate. The delegation of powers by the CEO is subject to the limits and restrictions set out in Section 3 of this Charter.

### Directors

- An executive director is a paid employee of the Company, and is [likely] a member of the senior management team of the Company. He or she is expected to add value to the Board's decision-

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### ► 21. Appendices

making process through their technical expertise and knowledge of the business and its industry.

- A non-executive director is not employed by the Company, but is not considered independent. He or she is expected to:
  - a) Constructively challenge and contribute to the development of strategy
  - b) Satisfy him or herself that the financial information is accurate and the risk management systems are robust.
- An independent non-executive director, in addition to the roles expected of a non-executive director, is not an employee of the Company. He or she is not a member of the management team, and is free of any business or other relationship that could materially interfere with the independence of their judgement.

In discharging his or her duties, each director is expected to:

- a) Exercise due care and diligence
- b) Act in good faith in the best interests of the Company
- c) Not improperly use his or her position or misuse information of the Company
- d) Commit the time necessary to discharge effectively his or her role as a director.

In addition, all directors, including executive directors, are entitled to be heard at all meetings and should bring an independent judgement to bear in decision-making.

Non-executive directors should also confer at least annually without the management's presence.

Collectively, the Board is ultimately responsible for the sustainability processes and report of the company.

## 5. Authorities Delegated to Senior Management Delegation to the CEO

The Board has delegated to the CEO authority over the day to day management of the Company, its subsidiaries and their respective operations [where applicable]. This delegation of authority includes responsibility for:

- a) Developing business plans, budgets and company strategies for consideration by the Board and, to the extent approved by the Board, implementing these plans, budgets and strategies
- b) Identifying and managing operational, strategic, financial, information technology and compliance risks (including material ESG risks) on a daily basis and, where those risks could have a material impact on the Company's businesses, formulating strategies for managing these risks for consideration by Board
- c) Managing the Company's current financial and other reporting mechanisms as well as its control and monitoring systems to ensure that these mechanisms and systems capture all relevant information on a timely basis and are functioning effectively
- d) Ensuring that the Board and its various committees are provided with sufficient information on a timely basis in regard to the Company's business and, in particular, with respect to the Company's performance, financial condition operating results, ESG performance, and prospects, to enable the Board and those committees to fulfil their governance responsibilities
- e) Implementing the policies, processes and codes of conduct approved by the Board.

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### ► 21. Appendices

### Reserved Powers

Any responsibilities not specifically delegated by the Board to the CEO or through him to Heads of Department, remain the responsibility of the Board.

## 6. Composition and Independence

### Board Composition

The Board consists a mix of executive and non-executive directors, with the majority being independent non-executive directors. This composition balances innovative thinking with general knowledge and experience.

### Director Independence

The Board has adopted a formal policy for the determination of the independence of its non-executive directors. The key criteria in the policy include:

- a) Independence from management; and
- b) Absence of any business relationship which could materially interfere with the director's independence of judgement and ability to provide a strong, valuable contribution to the Board's deliberations, or which could interfere with the director's ability to act in the best interests of the Company.

Should any contract exist, in the ordinary course of business, between the Company and another company in which a director has declared an interest, these will be reviewed for materiality to both the Company, and the other party to the contract.

## 7. Appointment and Removal of Directors

The Board should be of a size and composition that is conducive to making decisions expediently, with the benefit of a variety of perspectives and skills, and in the

best interests of the Company as a whole rather than of individual shareholders or other stakeholders.

The Nominations Committee is responsible for making recommendations to the Board relating to the appointment and retirement of directors.

A new director will receive a formal Letter of Appointment setting out the key terms and conditions relative to the appointment.

## 8. Board Structure

### Committees

To assist the Board in fulfilling its duties and responsibilities, it has established the following committees with the respective delegations:

#### *Nominations Committee*

- a) Board appointments, re-elections and performance
- b) Diversity obligations
- c) Director's induction programmes and continuing development
- d) Committee membership
- e) Succession of the CEO.

#### *Remuneration Committee*

- a) Remuneration and incentive framework for the Chairman, CEO, executive and non-executive directors and members of the senior executive management
- b) Strategic human resources policies.

#### *Audit Committee*

- a) Integrity of the Company's financial reporting
- b) Compliance with relevant legal and regulatory obligations

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
- 21. Appendices

- c) The effectiveness of the Company's enterprise-wide risk management and internal control framework
- d) Oversight of the independence of the external and internal auditors.

### *Board Risk Committee*

- a) Review and approve the risk management policy for approval by the Board
- b) Oversee the implementation of the risk management framework
- c) Review management's plans for mitigation of the material risks faced by the company
- d) Monitor emerging risks and changes in the risk profile
- e) Promote awareness of a risk-based culture.

## 9. Assessment and Evaluation of Board's

### **Performance**

Every year, an exercise takes place to evaluate the effectiveness of the Board, Board committees and individual directors. In accordance with best practices, the evaluation should be carried out at least every three years by an independent external facilitator. An external evaluation was carried out in [FY20XX], the outcome of which is discussed in more detail in the Company's [FY20XX].

### **The Chairman**

The Chairman's performance is evaluated by the non-executive directors, with input from members of the executive. The process is led by the senior independent non-executive director.

### **Executive Directors**

The CEO undertakes a performance evaluation of the other executive directors, with input from the Chairman and the non-executive directors.

### **Non-Executive Directors**

In years when the evaluation is conducted internally, the Chairman appraises the performance of non-executive directors and provides feedback on each individual's performance and contributions.

## 10. Remuneration Policies

### **Chairman**

It is the Company's policy that the Chairman should be remunerated on a competitive basis and at a level which reflects his contribution to the Company, as assessed by the Board. The Chairman is not present at any discussion regarding remuneration. The Chairman receives a fixed annual fee and does not receive any additional fee or allowance for either committee membership or for overseas travel.

### **Non-Executive Directors**

Fees paid to non-executive directors reflect their respective duties and responsibilities. They also reflect the time required to be spent by them to make a meaningful and effective contribution to the Company's affairs.

Non-executive directors receive a fixed annual fee. This comprises a base fee, committee membership or committee Chairmanship fees (where applicable), and allowances for attending meetings which involve air travel.

The fees are subject to review by the Chairman's Committee.



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
- 21. Appendices

### 11. Shareholder's Engagement

#### Shareholder Communications Policy

The Company has in place a shareholder communications policy to promote effective communication with shareholders and encourage effective participation at General Meetings.

Beneficial owners of the Company's shares are encouraged to contact the Company's [title of relevant department] to arrange the direct receipt of shareholder materials.

#### Tools of Shareholder Communications

As part of the Company's shareholder communications policy, the Company has employed the usage of the following platforms:

- a) Communication of information via the Internet: The Company will maintain its corporate governance website and make available – via its investor website – materials presented at significant investor briefings
- b) Annual report and circulars: Vital information regarding the Company's affairs in the business will be disclosed in the annual report. In addition, circulars will be provided as and whenever necessary to keep shareholders informed about the Company's latest strategic decisions.

### 12. Board Meetings

#### Agenda

The Chairman and Company Secretary should take responsibility for the content of the agenda, seeking input from other attendees such as other committee members, the CEO and senior management.

The agenda should provide an overview of the content, the ordering of items, the allocation of time for each item and deciding on invitees. A timed agenda will assist directors in recognising the relative significance of each issue and ensure the meeting is effective productive.

#### Meeting Attendance

Attendance at meetings is part of discharging the duties of a director. Directors should be present for Board and appropriate committee meetings. Absenteeism will never excuse a director from their duties to the Company.

The number of meetings of the Board and Board committees held in the year, as well as the attendance of every Board member at these meetings, will be disclosed in the Company's annual report.

### 13. Review of Charter

The Chairman of the Company will be the arbiter for interpretation and clarification of this Board Charter and issues pertaining to delegations of authority. Omissions should also be brought to the attention of the Chairman.

This Board Charter is subject to amendment by the Board. The Board will conduct periodic reviews of this Charter so as to ensure it remains relevant to the circumstances of the Company.

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
- 21. Appendices

### Appendix 2: Example Board annual agenda

The Board annual agenda should be designed as a practical work plan where the Board's staple business items are allocated to a particular meeting.

The example annual agenda below is one approach to the categorisation of business items and their allocation to specific meetings. In this example, it is assumed there will be 12 meetings of the Board, including an annual agenda is to achieve balance in the Board's workload through the year and ensure all Board responsibilities are attended to. The items of business have been categorised as follows:

- Matters that the Board has resolved for its decision (reserved authorities)
- Matters which have been delegated (e.g. to the CEO or a Board committee) (delegated authorities)

- Matters that are purely for information and do not require a Board decision (reporting)
- Procedural matter that may arise at any or every Board meeting (matters that may be applicable to all meetings).

The matters listed in the annual agenda and the scheduling for such matters will vary from company to company. Each Board should identify the core matters for inclusion in the annual agenda. As well as the anticipated Board business, there will be other matters which arise that require the Board's attention, such as a merger or acquisition or major capital expenditure. An annual agenda may be set out in many different ways. A different format is provided in [Appendix 4 \(example Audit Committee and annual agenda\)](#).

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
- 21. Appendices

## EXAMPLE BOARD ANNUAL AGENDA WORK PLAN

|                  | Reserved authorities   | Delegated authorities  | Reporting  | Matters that may be applicable to all meetings  |
|------------------|--|--|--|---|
| <b>Meeting 1</b> | <ul style="list-style-type: none"><li>• Board charter</li><li>• Annual agenda</li><li>• Retained authorities</li><li>• Delegated authorities</li><li>• Chairman, individual director and committee roles</li><li>• Company Secretary's role</li><li>• Advisory Boards</li><li>• Full-year or interim financial reporting</li><li>• CEO's position description and goal setting</li></ul> | <ul style="list-style-type: none"><li>• Investor relations strategy</li><li>• Management delegations, accountability and approval levels</li><li>• Board and management information system</li><li>• Strategic plan (actions and accountabilities)</li></ul> | <ul style="list-style-type: none"><li>• Regulatory and compliance report</li><li>• CEO/CFO report</li></ul>  | <ul style="list-style-type: none"><li>• Conflict and disclosure of interests</li><li>• Litigation and non-compliance issues</li><li>• Insider trading</li><li>• Share trading</li><li>• Continuous disclosure</li><li>• Access to company records</li><li>• Meeting agenda/papers/ preparation/ procedures/ decision-making processes</li><li>• Independent professional advice</li></ul> |
| <b>Meeting 2</b> | <ul style="list-style-type: none"><li>• Board and committee succession planning</li><li>• Risk appetite and risk management policy</li></ul>   | <ul style="list-style-type: none"><li>• Risk management strategy</li><li>• Risk profile and assessment</li><li>• Management accountability for risk</li><li>• Internal control environment</li></ul>   | <ul style="list-style-type: none"><li>• Regulatory and compliance report</li><li>• CEO/CFO report</li><li>• Audit committee report</li><li>• CEO/CFO report</li><li>• Major project reports</li><li>• Risk management report</li></ul> | <ul style="list-style-type: none"><li>• Protocols for Board/ management interaction between Board/ committee meetings</li><li>• Decision-making outside the boardroom (circular resolutions)</li><li>• Board minutes</li><li>• In-camera minutes</li><li>• Board member induction and education</li></ul>   |
| <b>Meeting 3</b> | <ul style="list-style-type: none"><li>• CEO succession planning</li><li>• Board training plan</li><li>• Corporate planning and budgeting</li></ul>   | <ul style="list-style-type: none"><li>• Reporting and communications strategy</li><li>• Review of key policies and procedures</li></ul>  | <ul style="list-style-type: none"><li>• Investor relations report</li><li>• Remuneration committee report</li><li>• CEO/CFO report</li></ul>   |   |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
- 21. Appendices

|                  | Reserved authorities  | Delegated authorities   | Reporting  | Matters that may be applicable to all meetings |
|------------------|---|---|--|--|
| <b>Meeting 4</b> | <ul style="list-style-type: none"> <li>• Director appointments/re-election</li> <li>• Director remuneration policy</li> <li>• Non-executive director remuneration</li> <li>• Director independence</li> <li>• Review of constitution</li> </ul> | <ul style="list-style-type: none"> <li>• Code of conduct</li> <li>• WH&amp;S plan</li> <li>• Corporate budgeting and planning</li> </ul>  | <ul style="list-style-type: none"> <li>• Regulatory and compliance report</li> <li>• CEO/CFO report</li> </ul>                                   | -  |
| <b>Meeting 5</b> | <ul style="list-style-type: none"> <li>• CEO performance review</li> <li>• Directors' insurance cover review</li> </ul>   | <ul style="list-style-type: none"> <li>• Stakeholder management update</li> <li>• Independent assurance provider performance review</li> <li>• Accountabilities framework update</li> </ul> | <ul style="list-style-type: none"> <li>• Sustainability/Corporate Social Responsibility report</li> </ul>  |  |
| <b>Meeting 6</b> | <ul style="list-style-type: none"> <li>• Assurance map</li> <li>• Half-year strategy review</li> </ul>  | <ul style="list-style-type: none"> <li>• Crisis management and continuity plan</li> <li>• CSR strategy</li> </ul>   | <ul style="list-style-type: none"> <li>• Investor relations report</li> <li>• Nominating committee report</li> <li>• CEO/CFO report</li> </ul>   |  |
| <b>Meeting 7</b> | <ul style="list-style-type: none"> <li>• Related party transactions</li> <li>• CEO/CFO attestations</li> </ul>  | <ul style="list-style-type: none"> <li>• Management attestations</li> </ul>   | <ul style="list-style-type: none"> <li>• Regulatory and compliance report</li> <li>• Audit committee report</li> <li>• CEO/CFO report</li> </ul> |  |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
- 21. Appendices

|                   | Reserved authorities  | Delegated authorities   | Reporting  | Matters that may be applicable to all meetings |
|-------------------|---|---|--|--|
| <b>Meeting 8</b>  | <ul style="list-style-type: none"> <li>• Director retirement/removal</li> <li>• Statutory reporting</li> </ul>  | <ul style="list-style-type: none"> <li>• Capital management strategy</li> </ul>                     | <ul style="list-style-type: none"> <li>• Remuneration committee report</li> <li>• Whistle-blower report</li> <li>• CEO/CFO report</li> <li>• Major projects report</li> <li>• Risk management report</li> <li>• External audit report</li> </ul> | -  |
| <b>Meeting 9</b>  | <ul style="list-style-type: none"> <li>• CEO appraisal</li> <li>• Executive remuneration</li> <li>• CEO and senior executive service agreements</li> <li>• Annual report and accounts, including directors' statement, solvency declaration and corporate governance statement</li> </ul> | <ul style="list-style-type: none"> <li>• Management and staff remuneration and HR policy</li> </ul> | <ul style="list-style-type: none"> <li>• Investor relations report</li> <li>• Audit committee report</li> <li>• CEO/CFO report</li> </ul>  |  |
| <b>Meeting 10</b> | <ul style="list-style-type: none"> <li>• Dividend policy</li> <li>• AGM documentation</li> <li>• Shareholder profiling</li> <li>• External audit independence, appraisal, retention, appointment and remuneration</li> </ul>  | <ul style="list-style-type: none"> <li>• Compliance program</li> </ul>                              | <ul style="list-style-type: none"> <li>• CEO/CFO report</li> </ul>   |  |



## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
- 21. Appendices

|  | Reserved authorities   | Delegated authorities   | Reporting  | Matters that may be applicable to all meetings |
|--|--|---|--|--|
| <b>Meeting 11</b>  | <ul style="list-style-type: none"> <li>Board and individual director evaluation</li> <li>Committee evaluation</li> </ul> | <ul style="list-style-type: none"> <li>Tax strategy</li> </ul>                                  | <ul style="list-style-type: none"> <li>Regulatory and compliance report</li> <li>Audit committee report</li> <li>CEO/CFO report</li> <li>Major projects report</li> <li>Risk management report</li> <li>Analyst and institutional presentations</li> </ul> | -  |
| <b>Meeting 12<br/>Board/<br/>management<br/>strategy day</b> | <ul style="list-style-type: none"> <li>Corporate objectives and strategic direction</li> </ul>                           | <ul style="list-style-type: none"> <li>Business model</li> <li>Strategic initiatives</li> </ul> | <ul style="list-style-type: none"> <li>Report on strategic execution/ success/ outcomes</li> <li>Draft strategic plan</li> </ul>   |  |

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
- 21. Appendices

### Appendix 3: Sample Audit and Risk Committee ("ARC") Charter<sup>268</sup>

#### Objective

To support the Board fulfil its oversight responsibilities in the following areas of:

- Financial statement preparation and integrity
- Risk management and internal controls (in relation to financial, operational, compliance, sustainability and information technology controls)
- Internal audit (resources, performance and scope of work)
- External audit (qualifications, independence, engagement and fees)
- ESG performance reporting.

Additional delegation of responsibilities to the ARC may include the following:

- Compliance (legal, regulatory and company policies)
- Interested persons transactions ("IPTs")
- Material sustainability risks and opportunities.

#### Authority

The ARC is authorised<sup>269</sup> by the Board to:

- Assist the Board in fulfilling its roles and responsibilities in accordance with the Terms of Reference detailed in this document
- Seek any information that it requires from any employee of the company in order to perform its duties

- Have direct and unrestricted access to the representatives of the external auditor (s), Head of IA, and management
- Meet with any relevant person of the company without the executive manager present, if necessary
- Obtain professional advice at the company's expense whenever deemed necessary<sup>270</sup>.

#### Membership

The Board shall appoint an ARC that has sufficient and relevant expertise to fulfil its role effectively<sup>271</sup>.

The ARC shall consist of the following:

- At least three directors
- Be composed exclusively of non-executive directors
- Have a majority of its members, including the ARC Chairman, as independent<sup>272</sup>.

New ARC members shall receive an induction covering the ARC's Terms of Reference, and be provided with an overview of the risk management and internal control systems.

The ARC members are required to keep abreast of changes in accounting standards and issues which have a direct impact on financial statements<sup>273</sup>.

#### Secretary

The Secretary of the company shall be the Secretary of the ARC.

<sup>268</sup> Guidebook for ACs, Appendix A2

<sup>269</sup> CG Code Guideline 12.3

<sup>270</sup> CG Code Guideline 6.5

<sup>271</sup> CG Code Guideline 12.2

<sup>272</sup> CG Code Guideline 12.1

<sup>273</sup> CG Code Guideline 12.8

## Foreword

01. Directors' Legal Duties
02. Structuring an Effective Board
03. Company Leadership
04. Productive Meetings
05. Ethical Culture
06. Board's Governance Roles and Conduct of Affairs
07. Insightful Strategy
08. Risk Management and Internal Controls
09. Board Committees
10. Receiving Assurance
11. Integrated Governance
12. Accountability to Shareholders
13. Stakeholder Engagement
14. Private Equity
15. Establishing a New Board
16. Managing Cybersecurity Risks
17. Corporate sustainability
18. Social media
19. Investment committees
20. Workplace safety & health
- 21. Appendices

### Meetings

The ARC shall meet at least four times a year at appropriate times in the company's reporting and audit cycle and whenever deemed necessary.

Attendance by all ARC members at each meeting is expected, whether in person or via telephone or video conference. The ARC will invite members of management (e.g. CEO, CFO), auditors (e.g. Head of IA, external auditor) or others (e.g. Non-Executive Directors, subject matter experts) to attend meetings and provide pertinent information, as necessary.

The ARC will meet separately, periodically (at least annually) with management. The ARC shall meet (a) with the external auditors, and (b) with the internal auditors, in each case without the presence of management, at least annually<sup>274</sup>. The external auditors and internal auditors may request a meeting whenever deemed necessary.

Meeting agendas will be prepared and provided in advance to members, along with appropriate briefing materials. Minutes will also be prepared.

### Reviews

To ensure that the ARC is fulfilling its stewardship duties to the Board, the ARC will:

- review, at least annually, the ARC Terms of Reference and recommend to the Board any appropriate amendments for approval
- review the annual agenda incorporating any changes in the Terms of Reference
- agree and review its key performance metrics with the NC with respect to how it discharges its roles and responsibilities

- conduct an annual assessment of its performance against its Terms of Reference duties and responsibilities and provide a report of the findings to the Board<sup>275</sup>
- conduct an annual assessment of each ARC member (the ARC Chairman should provide a report of the findings to the NC and Board Chairman)<sup>276</sup>.

### Reporting Requirements

In addition to providing the Board with a copy of the agenda, committee papers and minutes of its meetings, the ARC will ensure that:

- the ARC Chairman reports to the Board on ARC meetings, regarding all relevant matters and appropriate recommendations, in a written report (with supporting material) for noting or approval by the Board
- the ARC addresses any other reporting responsibilities.

### Responsibilities

The Board shall appoint an ARC that has sufficient and relevant expertise to fulfil its role effectively<sup>277</sup>.

#### i) Overseeing Financial Reporting

- Monitor the integrity of the financial information provided by the company, in particular by reviewing the relevance and consistency of the accounting standards used by the company (i.e. entity level) and its group (i.e. consolidation level)
- Assess, and challenge, where necessary, the accuracy, completeness, and consistency of financial information (including interim reports) before submitting to the Board for approval or made public

<sup>275</sup> CG Code Principle 5

<sup>276</sup> CG Code Principle 5

<sup>277</sup> CG Code Guideline 12.2

<sup>274</sup> CG Code Guideline 12.5

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### ► 21. Appendices

- Review the assurance provided by the CEO/CFO regarding the financial records being properly maintained and the financial statements giving a true and fair view of the company's operations and finances<sup>278</sup>.
- ii) **Overseeing Risk Management and Internal Controls (in relation to financial, operational, compliance, and information technology controls)**
  - Review the company's levels of risk tolerance and risk policies, and oversee management in the design, implementation and monitoring of the risk management and internal control systems<sup>279</sup>
  - Review the company's risk profile/risk dashboard on a regular basis to understand the significant risks, including material ESG factors, facing the company and how they are being mitigated
  - At least annually, review the adequacy and effectiveness of the risk management and internal control systems (including understanding the linkage between risks, controls and sources/evidence of assurance) with respect to financial, ESG, operational, compliance and information technology controls<sup>280</sup>. This may include reviewing management and/or assurance provider reports (e.g. IA) to highlight significant findings and recommendations, inclusive of management's responses
  - Review the assurance provided by the CEO/CFO regarding the effectiveness of risk management and internal controls<sup>281</sup>

<sup>278</sup> CG Code Guideline 11.3

<sup>279</sup> CG Code Guideline 11.1

<sup>280</sup> CG Code Guideline 11.2

<sup>281</sup> CG Code Guideline 11.3

- Prepare ARC report regarding the adequacy and effectiveness of risk management and internal control systems to the Board (as part of SGX Listing Rule 1207 (10) requirements and Principle 11 of the Code of Corporate Governance)
- Review disclosures in the annual report relating to the adequacy and effectiveness of the risk management an internal control systems<sup>282</sup>
- Review the company's procedures for detecting fraud and whistleblowing, and ensure that arrangements are in place by which staff of the company and any other persons may, in confidence, raise concerns about possible improprieties in matters of financial reporting, financial control, or any other matters<sup>283</sup>.

### iii) **Overseeing Internal Audit**

- Monitor and assess the role and effectiveness of the IA function<sup>284</sup> (including the IA charter, plans, activities, staffing, budget, resources, and organisational structure of the IA function)
- Conduct internal quality assurance review (QAR) of the IA function at least annually<sup>285</sup>. Conduct independent validation of QAR at least once every five years
- Where the QAR identifies the gaps/ lack of expertise with the existing IA function, the AC may consider co-sourcing or outsourcing options for the IA function
- Review the IA program and reports on a periodic basis and monitor management's responsiveness to the findings and recommendations
- Ensure that the Head of IA has direct and unrestricted access to the Chairman of the Board and ARC, and is able to meet separately and privately to discuss matters/concerns<sup>286</sup>

<sup>282</sup> CG Code Guideline 11.3

<sup>283</sup> CG Code Guideline 12.7

<sup>284</sup> CG Code Guideline 12.4

<sup>285</sup> CG Code Guideline 13.5

<sup>286</sup> CG Code Guideline 13.1

## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### ► 21. Appendices

- Participate in the appointment, replacement or dismissal of the Head of IA<sup>287</sup>.

#### iv) Overseeing External Audit

- Oversee the company's relations with the external auditor (including audit scope, approach and fees)<sup>288</sup>
- Review the performance of the external auditors, to facilitate the selection, appointment, re-appointment, and resignation (e.g. assess effectiveness through level of errors identified, accuracy in handling key accounting audit judgment, and response to queries from the ARC)<sup>289</sup>
- Monitor and assess annually the external auditor's independence or objectivity is not impaired (including the amount of fees and the provision of non-audit services)<sup>290</sup>
- Review the audit representation letter (particularly in relation to non-standard issues) and the external auditor's management letter to assess whether it is based on a good understanding of the company's business, and monitor the responsiveness of management to the recommendations made (or the reasons why they have not been acted upon)
- Establish regular meetings with the external auditor to discuss matters that the ARC or auditors believe should be discussed privately
- Ensure that the external auditors have direct and unrestricted access to the Chairman of the ARC and the Chairman of the Board.

287 CG Code Guideline 13.1

288 CG Code Guideline 12.4

289 CG Code Guideline 12.4

290 CG Code Guideline 12.6

## Additional Responsibilities (as required)

The following additional responsibilities may be delegated to the ARC:

### i) Compliance

- Review the effectiveness of the system for monitoring compliance with laws and regulations and the results of management's investigation and follow up of any instances of non-compliance
- Monitor the processes for addressing complaints made regarding accounting, internal controls and/or auditing matters
- Clarify the company's code of conduct and process for disseminating requirements across all company personnel and monitoring levels of compliance
- Maintain open communication with and receive periodic reports from management and company legal counsel regarding compliance matters.

### ii) Interested Persons Transactions

- Review IPTs to consider whether they are on normal commercial terms and are not prejudicial to the interests of the company or its minority shareholders
- Determine methods or procedures for determining the transaction prices are sufficient to ensure that the transactions will be carried out on normal commercial terms and not prejudicial to the issuer
- Direct management to present the rationale, cost-benefit analysis and other details relating to IPTs subject to a specific mandate
- Receive reports from management and IA regarding IPTs. Report to shareholders on IPTs as required by the Listing Manual.



## Foreword

### 01. Directors' Legal Duties

### 02. Structuring an Effective Board

### 03. Company Leadership

### 04. Productive Meetings

### 05. Ethical Culture

### 06. Board's Governance Roles and Conduct of Affairs

### 07. Insightful Strategy

### 08. Risk Management and Internal Controls

### 09. Board Committees

### 10. Receiving Assurance

### 11. Integrated Governance

### 12. Accountability to Shareholders

### 13. Stakeholder Engagement

### 14. Private Equity

### 15. Establishing a New Board

### 16. Managing Cybersecurity Risks

### 17. Corporate sustainability

### 18. Social media

### 19. Investment committees

### 20. Workplace safety & health

### ► 21. Appendices

### Appendix 4: Example Audit Committee annual agenda

A comprehensive documented annual agenda assists the Audit Committee to discharge its duties in a coordinated manner. The following provides a suggested example of an Audit Committee annual agenda.

|  | SCHEDULED MEETINGS |     |     |     |
|--|--------------------|-----|-----|-----|
| ASSUMING FINANCIAL YEAR-END 31 DECEMBER  | FEB                | MAY | AUG | NOV |
| <b>Assess Financial Information</b>  |                    |     |     |     |
| Review significant accounting and reporting issues and assess material financial estimates and assumptions used  |                    |     |     |     |
| Review and approve quarterly financial statements and announcements  |                    |     |     |     |
| Review budget and forecasts  |                    |     |     |     |
| Review conflicts of interest, interested and related party transactions  |                    |     |     |     |
| <b>AC Composition and Effectiveness</b>  |                    |     |     |     |
| Review AC charter, annual agenda and attendees   |                    |     |     |     |
| Assess AC composition including individual member's performance, qualifications (E.g. financial literacy, skills and experience) and member rotation/succession planning   |                    |     |     |     |
| <b>Risk management and internal controls</b>   |                    |     |     |     |
| Assess requirements of SGX listing rule 1207 (10) and Code of Corporate Governance Principle 11 regarding adequacy and effectiveness of: risk management (e.g. risk profile, risk appetite) and internal controls (e.g. IA and CSA findings and results) |                    |     |     |     |
| Review CEO/CFO assurance to Board regarding effectiveness of risk management and internal control  |                    |     |     |     |
| <b>External auditors</b>   |                    |     |     |     |
| Recommend appointment and re-appointment and evaluation of the external auditors (including review of fees, provision of non-audit services, objectivity/independence, review of audit plan)   |                    |     |     |     |
| Review external auditor's report, findings and progress on management actions (discuss issues with auditor in the absence of Management)   |                    |     |     |     |
| <b>Internal auditors</b>   |                    |     |     |     |
| Review IA charter (if necessary), approve appointment of IA and review performance   |                    |     |     |     |
| Review IA plan (including progress, implementation of Management actions, changes to the plan and/or resource issues) - discuss issues with the internal auditor in the absence of Management  |                    |     |     |     |
| <b>Compliance and other responsibilities (If delegated to the AC)</b>  |                    |     |     |     |
| Review legal and regulatory matters that may have a material impact on the company   |                    |     |     |     |
| Review compliance report from management, and correspondence (if any) from regulatory bodies (with a material impact on the company)   |                    |     |     |     |
| Review whistleblowing arrangements and reports as well as irregularities (including fraud) reports   |                    |     |     |     |
| Conduct special investigations and perform other activities, as appropriate  |                    |     |     |     |
| <b>Reporting</b>   |                    |     |     |     |
| Maintain minutes and report to the board   |                    |     |     |     |

Source: Guidebook for ACs, Appendix B1

Recommended Timing As required

\*links in document are correct as of Sept 1 2016

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