



**SID**  
SINGAPORE  
INSTITUTE OF  
DIRECTORS

# The Singapore Directors' Toolkit

VERSION 1.0

November 2014



## Director's Toolkit Overview

1. Directors' Legal Duties
2. Structuring an Effective Board
3. Company Leadership
4. Productive Meetings
5. Ethical Culture
6. Board's Governance Roles and Conduct of Affairs
7. Insightful Strategy
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# Foreword

Our business environment presents a fast moving 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, a more intense pace of technological innovation and digitisation, and a more rigorous regulatory environment.

At the same time there is more focus on directors' duties, roles and responsibilities in light of increased regulatory changes. Directors play a critical role in shaping the corporate governance culture and framework within companies. Greater understanding of the requirements and how to apply them in practice is essential to improve governance standards.

To support directors in their challenging role, KPMG in Singapore and the Singapore Institute of Directors (SID) have jointly developed The Singapore Directors' Toolkit. This 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.

The Toolkit is intended to be updated and revised from time to time. It provides useful case studies of real-life examples on how to deal with complex and challenging issues. We trust that our members, as key custodians of the oversight role, will find this Toolkit an important resource. As always, we welcome any suggestions for improvements as we seek to serve our members better.

**Irving Low**  
Partner, KPMG



**Willie Cheng**  
Chairman, Singapore Institute of Directors



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## About SID

SID's mission is to promote the professional development of directors and corporate leaders and encourage the highest standards of corporate governance and ethical conduct. SID's vision is to be the national association advancing the highest level of ethical values, governance, and professional development of directors. Since its formation in 1998, SID has continued to play a crucial role in the promotion and development of good corporate governance practices and the professional education of directors.

With over 2,000 members today, SID is well regarded as the national professional body for directors serving the local corporate community and contributing to the international corporate governance agenda.

The Institute continues to provide thought leadership on corporate governance and directorship issues in Singapore. SID regularly produces articles and publications of interest to directors and corporate leaders including the quarterly SID Directors' Bulletin, to keep directors abreast of current issues, and "boardroom Matters", a weekly column which appears in The Business Times and BT Invest.

SID provides a full range of training programmes, seminars and events for the ongoing professional development of its members, and also to increase and encourage a larger pool of individuals qualified to serve as directors. It also organises regular talks, forums and seminars throughout the year on current topics of interest to members. For more information, please visit [www.sid.org.sg](http://www.sid.org.sg) or contact the SID Secretariat at (65) 64221188.

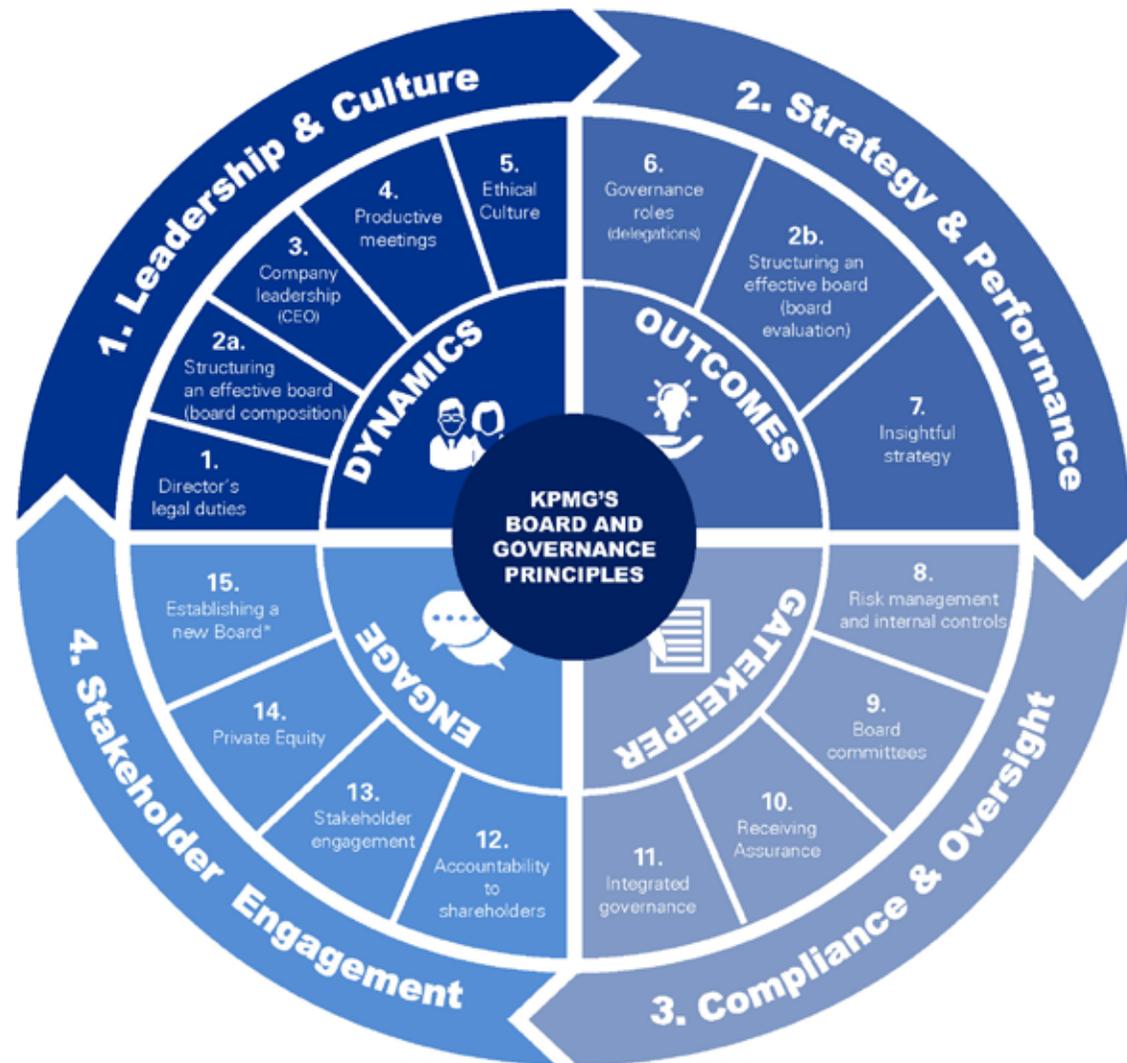
## About KPMG

KPMG in Singapore is a member firm of the KPMG global network of professional services firms providing Audit, Tax and Advisory services. KPMG member firms operate in 156 countries and collectively employ over 155,000 people across a range of disciplines. We contribute to the effective functioning of international capital markets and we support reforms that strengthen the markets' credibility and social responsibility. Drawing on industry insight and technical knowledge, our professionals assist clients in their pursuit of business growth, enhanced performance, governance and compliance objectives. KPMG in Singapore has established the KPMG Audit Committee Institute and the Board and Governance Institute to provide regular thought leadership to boards and C-Suite executives on current and emerging topics. For more information, please visit [www.kpmg.com.sg](http://www.kpmg.com.sg)

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# Directors' Toolkit Overview



\* This chapter requires elements from all parts of the Toolkit to be present

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# 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)?
2. Does the Board receive reports from management about material changes to laws, regulations, Listing Manual and CG Code?
3. Am I fully aware of my duties and responsibilities regarding conflicts of interest?
4. Is there an effective procedure for identifying and disclosing related party transactions and interested party transactions?
5. Is the Board immediately advised of queries received from the SGX or other regulators?
6. Are directors' interests properly disclosed in the financial statements and directors' report?
7. Do I understand the scope and limitations of the directors' and officers' liability insurance policy?
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

1. The company's Memorandum and Articles of Association is never, or rarely, referred to in Board discussions or documentation
2. Certain directors are perceived to have conflicts of interest
3. Concern that a family member of a director is a senior executive of a major supplier or customer
4. 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)
5. A director lets price sensitive information slip
6. Insider trading by an employee is discovered, but no action is taken
7. Concerns about certain directors or officers trading in company securities immediately before public announcements
8. 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

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Directors' responsibilities are regulated and guided by the following:

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

and 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 to avoid situations where they are held responsible for breaching certain regulations, even when they did not specifically commit or authorise such a breach.

### Articles of Association

The power to control the affairs of the company is typically vested in the directors by the company's AoA. The provisions of the AoA are a key component of a company's governance framework. Directors should be familiar with the AoA 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 Main Board 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 and this would include de facto, shadow, alternate, independent, nominal, nominee, executive and non-executive directors<sup>2</sup>.

A director is responsible for providing the direction for the company. Directors must make decisions objectively and act in the best interest of the company, and be honest and diligent in carrying out your duties<sup>3</sup>.

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

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. Whilst 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'.

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

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

<sup>3</sup> CA Section 157

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A director owes his/her duties to the<sup>4</sup>:

- 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
- Employee - directors must consider the interests of the employees when exercising their powers
- 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.

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 interest of the company**

The director must act bona fide and in the best interests of the company instead of for personal gain, and must ensure transactions are commercially justifiable and not for improper purposes. A director is not entitled to make a personal profit or obtain personal advantage ("no profit" rule) by using company property and money, or with the company information acquired as a director. Directors must objectively make decisions in the interests of the company<sup>5</sup>. Directors must not act beyond powers given in the AoA, illegally or contrary to public policy.

An offence is committed under both statute and common law if it can be shown that the conduct was undertaken with the intention of gaining an advantage. It is not necessary to establish that the advantage was actually obtained.

<sup>4</sup> CA Section 159

<sup>5</sup> CG Code Principle 1.2

### **Duty of care and skill: to exercise care and skill reasonably expected of them**

A director is under a mandatory duty, at all times to act honestly and use reasonable skill, care and diligence in discharging his duties. 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 [*Jurong Readymix Concrete Pte Ltd v Kaki Bukit Industrial Park Pte Ltd [2000] 4 SLR 723*].

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.
  - 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 your company.

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## 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 ("Creanovate"). 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 addition, 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 but 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.*

*This case highlights the difference between negligence or wilful ignorance, 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 may have the opposite effect.*

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### Statutory duties

Directors should act honestly and diligently in discharging their duties and in compliance 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 receipts of notifications from its directors, reporting their discloseable interests and changes thereof
- S156 Duty to disclose interests in transactions (examples include interests in property or offices which may create conflict on interests)
- S164 Duty to disclose director's shareholdings (example 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 and directors' reports. Accounting records must comply with Accounting Standards.

Common defaults of statutory duties include failure to hold an AGM<sup>6</sup>, failure to file annual returns<sup>7</sup>, failure to file changes in particulars, especially resignation of directors<sup>8</sup> and change in company's registered office address<sup>9</sup>.

The SGX LR Chapter 7 sets out the continuing disclosure requirements which a listed company has to comply with. Reference should also be made to SGX's Corporate Disclosure Policy in Appendix 7.1.

<sup>6</sup> CA Section 175

<sup>7</sup> CA Section 197

<sup>8</sup> CA Section 173

<sup>9</sup> CA Section 143

<sup>10</sup> CA Section 163

### Conflict of interests and disclosure

A director should avoid being in a position where other interests or duties conflict with their duties to the company. Conflicts of interest can arise in several situations:

- Where directors have a direct or indirect material interest in transactions that the company enters into
- Where directors hold positions or offices or possess property that may result in conflicting duties
- Where directors stand to benefit from corporate information received by them or opportunities made available to them in their capacity as directors or officers.

In dealing with conflicts of interest, directors should pay close attention to:

- 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>10</sup>
- SGX LR Chapter 9
- Company's AoA.

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 a company now operates in. 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.

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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 actually 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.

Directors should be familiar with their duty to disclose conflicts under Section 156 of the CA and the company's AoA. The disclosure requirements are as follows:

- Disclosure of transactions with the company  
Appropriate disclosure has to be made to the Board if a director is interested in any of the transactions the company is undertaking or considering<sup>11</sup>. Such disclosure should be made at a directors' meeting and be recorded in the minutes.
- Disclosure of conflict arising from holding other offices  
A director is required to make disclosure if he holds any office or property where his interests are in conflict with his duties as a director in the company<sup>12</sup>.

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 AoA. However, in the absence of any prohibition in the AoA, 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 AoA prohibits directors from voting where the contract or proposed contracts in which the directors have, directly or indirectly, a personal material interest<sup>13</sup>.

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 for the directors to try to resolve the matter.

<sup>11</sup> CA Section 156(1)

<sup>12</sup> CA Section 156(5)

<sup>13</sup> SGX LR 409, Appendix 2.2 (9)(e)

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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.

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## CASE STUDY



*In the 2000 case of Public Prosecutor 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 in as director or shareholder.*

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

In Singapore, there are two main sources of rules governing related party and interested person transactions. These are FRS 24 on Related Party Disclosures and Chapter 9 of the SGX LR for SGX Main Board and Catalist companies.

Related party transaction requirements only 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 is a person or entity that is related to the entity that is preparing its financial statements; includes directors, substantial shareholder and CEO or person with significant influence<sup>14</sup>. 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>15</sup>.

Chapter 9 of the SGX LR regulates interested person transactions in order to minimise the risk that interested persons entering into transactions with the company, its subsidiaries or associated companies may adversely affect the interests of the company or its shareholders. In the case of a company, interested person means 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>16</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. 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. The rule does not apply to any transaction below S\$100,000<sup>17</sup>.

A 2013 survey by KPMG and NUS<sup>18</sup>, found that the most common type of IPT relationships 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 this 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 will be having directors to disclose their associates as accurately as possible on a periodic basis using a checklist to prevent unintentional omissions of significant relationships. The company should also work with its internal auditors to review the adequacy and effectiveness of using these checklists.

<sup>14</sup> FRS 24

<sup>15</sup> FRS 24

<sup>16</sup> SGX LR 904

<sup>17</sup> SGX LR 905 & 906

<sup>18</sup> *The Ties That Bind: Interested Person Transactions: Rules and Practices*, KPMG and NUS publication, September 2013, page 22

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## 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. is 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 highlights the conflict between his role as the Audit Committee Chairman and his firm's role in providing accounting-related services.*

*This followed China Sky's assertion of Mr. Lai's independence, after a 2010 corporate governance report that stated 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," it is highly questionable as to why the services of SK Lai & Co. were engaged, when there are many other accounting firms that can provide 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 had confirmed that the relationship between Mr. Lai's accounting services firm and China Sky constituted an IPT<sup>19</sup>.*

<sup>19</sup> <http://www.bloomberg.com/news/2012-04-18/china-sky-ex-director-takes-on-singapore-bourse-on-rebuke.html>

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### 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>20</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>21</sup>.

The following situations represent a breach of insider trading requirements<sup>22</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>23</sup>.

<sup>20</sup> SFA Section 218

<sup>21</sup> CA Section 157(2)

<sup>22</sup> SFA Section 218

<sup>23</sup> CA Section 161

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## CASE STUDY



*In 2011, the former Chief Operating Officer (COO) of Airocean, Johnson Chong ("Mr. 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, Judge Liew Thiam Leng 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>24</sup>.*

<sup>24</sup> <http://www.mondaq.com/x/134508/Directors+Officers+Executives+Shareholders/The+Airocean+Case>

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### Insolvent trading

Directors also have a duty to ensure that the company does not trade while it is insolvent. A company will be deemed insolvent if it is not able to pay its debts if and when they become due and payable<sup>25</sup>. They should look out 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 and insufficient maturity and liquidity analysis of the company's debt profile, should all raise concerns for directors.

A director should not contract a debt where he/she has no reasonable ground of the company being able to pay its debt at the time of contracting<sup>26</sup>. The director will be personally liable for the payment of that debt. Directors who knowingly consent to the company trading 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>27</sup>.

There is a defence that the director had reasonable grounds to expect, and did expect, that the company was solvent. This defence usually requires a careful assessment of the company's financial standing to determine whether it provided the director with the requisite 'reasonable grounds' to expect solvency. However, if a director of a company who makes a solvency statement without having reasonable grounds for the opinions expressed in it shall be guilty of an offence and shall be liable on conviction to a fine not exceeding \$100,000 or to imprisonment for a term not exceeding 3 years or to both<sup>28</sup>.

Insolvency, or the threat of insolvency, requires directors to act in the interest of creditors. It is a situation in which directors must subordinate the interests of shareholders

to those of the company's creditors. In this context, directors should note that the company must not pay a dividend except out of profits<sup>29</sup>.

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 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>30</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

<sup>25</sup> CA Section 149(5)

<sup>26</sup> CA Section 339(3)

<sup>27</sup> CA Section 340(5)

<sup>28</sup> CA Section 7A(6)

<sup>29</sup> CA Section 403

<sup>30</sup> SGX LR 703

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- 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 sub-contractors, 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.

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>31</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)

<sup>31</sup> SGX LR 1207(19)(b)

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- 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 – 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. 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 Duty to act honestly and with reasonable diligence	Fine not exceeding \$5,000 or imprisonment for a term not exceeding 1 year <sup>32</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>33</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 to imprisonment for a term not exceeding 7 years or to both.

<sup>32</sup> CA Section 157(3)(b)

<sup>33</sup> CA Section 156(10)

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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.

### Business judgement rule

There is no formal business judgement rule in Singapore. However in Vita Health Laboratories Pte Ltd & Ors v Pang Seng Meng [2004] 4 SLR(R) 162, it was stated that 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 faiths, it cannot be contended that directors are invariably liable by their failure in business judgment for all losses sustained by a company.

### Directors' indemnities and insurance

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>34</sup>. In addition, the AoA 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 AoA may be incorporated into an agreement between the company and each director since the AoA 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.

However, a company cannot by provisions of the AoA 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>34</sup> CA Section 172

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



## RED FLAGS

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

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### 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>35</sup>. There needs to be a formal and transparent process for the appointment and re-appointment of the Board members<sup>36</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 committees in ensuring that the company's current and long term strategies are fulfilled
- Enhancing communications amongst the Board member, 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>37</sup>.

### Skills and expertise

The Board should be made of a group of professionals with the right mix of skills 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 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>38</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 director's academic and professional qualifications should be disclosed in the company's annual report<sup>39</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.

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

<sup>35</sup> CG Code Principle 1

<sup>36</sup> CG Code Principle 4

<sup>37</sup> CG Code Guideline 4.4

<sup>38</sup> CG Code Guideline 1.6 & 5.3

<sup>39</sup> CG Code Guideline 4.7

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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 will be a blind gap 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 Board should 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>40</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 on Chairman's leadership skill and industry experience
- Enhancing director search and nomination process
- Placing importance of 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 a joint initiative between the Centre for Governance, Institutions and Organisations (CGIO) at NUS Business School and BoardAgender in November 2013 released interesting findings about female representation at the Board level. Gender diversity remains a challenge in Singapore's Boards. Women in Singapore still hold less Board positions compared to their counterparts in Indonesia, Malaysia, China, Hong Kong and Australia. The survey found that 8% of Board directors in SGX listed companies are women; with less than 5% of those being the CEO or Chairman. According to industry, gender diversity can be found most in the property and hotel/ restaurants, and least in manufacturing. The finance industry is seeing improvements in having women in the Board. In 2008, it was found that female representation on the Board was 6.6% with no significant improvements in 2013. Although the study showed positive relations between the ratio of women in the boardroom and the firms' Return on Assets and Return on Equity in the subsequent three years, the increase is not expected to improve markedly given the long tenure of directors in Singapore and the fact that very few directors are being replaced.

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.

### Board size

The Board is required to examine its size to enable it to effectively function 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>41</sup>.

<sup>40</sup> CG Code Guideline 2.6

<sup>41</sup> CG Code Guideline 2.5

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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 AoA 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 as well. 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 development<sup>42</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

experiences, 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>43</sup>
- Anyone who is automatically disqualified for up to 5 years if convicted of an offence involving fraud or dishonesty<sup>44</sup>
- Anyone who has a disqualification order made against him/her by a court
- Anyone who has 3 or more High Court Orders made against him/her compelling compliance with the relevant 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>45</sup>
- Anyone who is a director of an insolvent company<sup>46</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>47</sup>

<sup>42</sup> CG Code Principle 4

<sup>43</sup> CA Section 148

<sup>44</sup> CA Section 154(1)

<sup>45</sup> CA Section 155

<sup>46</sup> CA Section 149

<sup>47</sup> CA Section 149A

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### 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 Board representations. In addition, the director should enquire the company's policy on the maximum number of directorships which any director may hold<sup>48</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

<sup>48</sup> CG Code Guideline 4.4

<sup>49</sup> CG Code Guideline 1.7

- Ascertain if there has been any queries from regulatory authorities.
- Adequacy of director' D&O and remuneration package.

### Director letter of appointment

The new director should be issued with a letter of appointment<sup>49</sup>, setting out the terms and conditions of appointment, including:

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

### 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.

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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, the main issues for the company's business, 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>50</sup>.

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 utilise the company's resources to achieve the company's long term goals.

It is a tool for 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>51</sup>.

<sup>50</sup> CG Code Guideline 4.2(c)

<sup>51</sup> CG Code Principle 5

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### 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 on 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 a form of a questionnaire whilst others may engage an external party to conduct interviews.

<sup>52</sup> CG Code Principle 5.1

<sup>53</sup> CG Code Principle 5.2

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

- The objective of the evaluation is clear  
Boards must agree to a commitment on the purpose and process. Questions on roadblocks on 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 culture norms.
- A Board leader drives the process  
The Board performance is to be carried out by the NC with clear process of how with the basis of assessments being identified for approval by the entire Board<sup>52</sup>. The performance criteria should be comparable with other industry peers and should address how long term shareholder value can be enhanced<sup>53</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.

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- 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 reviewing 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 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.

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### 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 AoA.

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>54</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>55</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>56</sup>. 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>57</sup>.

Larger organisations will often develop a fee system that compensates directors according to the number of sub-committees 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. This should involve reviewing the director's remuneration annually 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>58</sup> should be provided in the annual report<sup>59</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>60</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-based incentives and other long term awards<sup>61</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>62</sup> as well as the link between remuneration paid to the executive directors and key management personnel, and performance<sup>63</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>64</sup>.

<sup>54</sup> CG Code Guideline 8.1

<sup>55</sup> CG Code Principle 8

<sup>56</sup> CG Code Guideline 8.2

<sup>57</sup> CG Code Guideline 8.3

<sup>58</sup> CG Code Guideline 9.2

<sup>59</sup> CG Code Guideline 9.1

<sup>60</sup> CG Code Guideline 9.3

<sup>61</sup> CG Code Guideline 9.2 & 9.3

<sup>62</sup> CG Code Guideline 9.4

<sup>63</sup> CG Code Guideline 9.6

<sup>64</sup> CG Code Guideline 9.5

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### Board succession planning

Board succession planning challenges Boards to anticipate and plan for their future needs. Such 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.

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 optimal Board composition should be reviewed by the Chairman with the assistance of the NC -

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/ she 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.

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## 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 searches for a new CEO. Ms. Catherine Lee, the CFO of SMRT had made a statement stating that although the search for a new CEO has 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 on the job, came after mounting public anger, and brought to light the room for improvement in SMRT's succession planning<sup>65</sup>.*

<sup>65</sup> <https://sg.news.yahoo.com/smrt-ceo-saw-phaik-hwa-resigns.html>

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### Access to company records

Directors should have access to complete, adequate and timely information of the company at all times so as to enable them to make informed decisions in discharging their duties<sup>66</sup>. Directors are entitled to request from management additional information as needed to make informed decision and the management shall provide required information in a timely manner<sup>67</sup>.

Information that management should furnish the directors include 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>68</sup>. Such information should be furnished to the Board monthly or/as and when required for the Board to make balanced and informed decision<sup>69</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.

### Director resignation, retirement and removal

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

A director is not allowed to resign or vacate his office (notwithstanding the provisions in the company's AoA or any agreement with his company) unless there is remaining in the company at least one director who is ordinarily resident in Singapore<sup>70</sup>. The company's AoA would provide the various situations in which a director may vacate the office. A company is required to remove a director by passing ordinary resolution before the expiration of his period of office<sup>71</sup>.

All directors should be required to undergo a re-nomination process and be re-appointment at regular intervals and at least once every three years<sup>72</sup>. The independence of the directors will need to be examined if they have served on the Board beyond 9 years<sup>73</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>74</sup>. Any director's resignation has to be announced immediately<sup>75</sup>.

<sup>66</sup> CG Code Principle 6

<sup>67</sup> CG Code Guideline 6.1 & 6.2

<sup>68</sup> CG Code Guideline 6.2

<sup>69</sup> CG Code Guideline 10.3

<sup>70</sup> CA Section 145(5)

<sup>71</sup> CA Section 152(1)

<sup>72</sup> CG Code Guideline 4.2

<sup>73</sup> CG Code Guideline 2.4

<sup>74</sup> SGX LR 704 7)

<sup>75</sup> SGX LR 704(8)

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## CASE STUDY



*China Sky's three independent directors, Er Kwong Wah, Yeap Wai Kong and Lai Seng Kwoon, resigned with immediate effect on 5th January 2012. This occurred following the company's non-compliance with SGX's directives to appoint a special auditor to investigate transactions between the company and its Audit Committee Chairman. The directors were of the view that there was no justification for the directive and the matter worsened when SGX escalated the case to the High Court to impose on China Sky and its directors to comply with these listing requirements<sup>76</sup>.*

<sup>76</sup> [http://www.china.org.cn/world/Off\\_the\\_Wire/2012-09/14/content\\_26529580.htm](http://www.china.org.cn/world/Off_the_Wire/2012-09/14/content_26529580.htm)

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



## RED FLAGS

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

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### 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.

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.

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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 cooperation 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.

### *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>77</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

<sup>77</sup> Booz and Co., *CEO Succession Report 2011 – 12th Annual Global CEO Succession Study*

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over the last 12 years, insider CEOs serve longer terms than outsider CEOs, with an average tenure of 7.6 years (compared to 5.6 years for 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/her 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. 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>78</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.

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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 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>79</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>80</sup>.

The Board should establish a formal and transparent procedure for developing policy on executive and director remuneration<sup>81</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>82</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 to<sup>83</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>84</sup>.

<sup>78</sup> CG Code Principle 7 and 8

<sup>79</sup> CA Section 169

<sup>80</sup> SGX LR 1207(15) and CG Code Principle 9

<sup>81</sup> CG Code Principle 7

<sup>82</sup> CG Code Guideline 7.2

<sup>83</sup> CG Code Guideline 7.3

<sup>84</sup> CG Code Guideline 8.4

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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.

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 AoA
- 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.

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



## RED FLAGS

1. Board or subcommittee meetings are not scheduled on a regular basis
2. Meeting agendas and materials are not circulated in advance, hence not allowing for adequate time for review
3. The Company Secretary provides incomplete or late distribution of Board meeting minutes after meetings
4. Many issues discussed are carried over to the next meeting
5. Attendee and absentee lists are kept irregularly and sometimes not noted in the minutes
6. There is no information sharing portal set up for the Board and directors rely on emails and handouts to communicate and store information
7. Meetings are usually closed without an agreed set of actions
8. The mode to exchange and store information and documents are not secured

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### 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 advanced 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 considering for re-election to the Board.

Unless the company's AoA provides otherwise, the quorum for a directors' meeting is two directors, and the quorum must be present at all times during the meeting<sup>85</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 AoA.

#### *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>86</sup>. The Chairman's key role is to lead discussions, encourage participation of and interaction amongst members anyone 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 Chairperson 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>87</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
- Meeting begins and ends 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.

#### *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.

<sup>85</sup> CA Section 179(1)(a)

<sup>86</sup> CG Code Guideline 3.2

<sup>87</sup> 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)

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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 having informed on 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. 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>88</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.

<sup>88</sup> CG Code Guideline 1.4

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### 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 effective Board functioning, 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.

### 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

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### 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.

### 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>89</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

<sup>89</sup> CA Section 188(3)(b)

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- Confidentiality issues and potential conflicts of interest
- Independence concerns relating to assurance providers
- Sensitive matters affecting management and/or assurance providers
- Internal audit/external auditor.

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>90</sup>. The company is required to retain records up to a period of 5 years<sup>91</sup>. The minutes must also be signed within a reasonable timeframe. The minutes shall be open for members to peruse without charge<sup>92</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 the level of attention it warrants, rather than simply treating it as an administrative exercise. Once signed, minutes are evidence of a proceeding, resolution or declaration to which it relate. 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 and if the minutes are amended at the next Board meeting, this should be reflected in the minutes of the subsequent meeting.

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>93</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).

<sup>90</sup> CA Section 188

<sup>91</sup> CA Section 199(2)

<sup>92</sup> CA Section 189

<sup>93</sup> CA Section 189(1)

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### 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.

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# 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>94</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?
2. Has the organisation's ethics and compliance program been reviewed by outside consultants or experts for possible improvement?
3. Have any compliance investigations arisen from a cultural problem?
4. Is there an effective whistle-blowing process in place?
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?
6. Has a corporate culture been developed and maintained that creates an environment of openness, honesty and the immediate reporting of bad news?
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?
8. Are there processes and practices in place to promote ethical behaviour?
9. Has the Board considered how executive compensation aligns with the desired ethics and compliance culture?



## RED FLAGS

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

<sup>94</sup> KPMG, *Survival of the Most Informed: GRC Comes of Age – How to Envision, Strategize, and Lead to Achieve Enterprise Resilience*, 2010.

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### '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>95</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>96</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>97</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.

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

<sup>95</sup> KPMG, *The Road to a Model Ethics and Compliance Program*, 2009.

<sup>97</sup> KPMG, *A view from the top – Business Ethics and Leadership*, 2005.

<sup>96</sup> CG Code Guideline 1.1(e)

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- 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.

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 conflict of interests.

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.

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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>98</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>99</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.

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.

<sup>98</sup> *20 Questions Directors Should Ask about Codes of Conduct*, Gunns. M & Wexler, M. 2010

<sup>99</sup> *K. M. Gilley, C. Robertson, T.C. Mazur, The bottom-line benefits of ethics code commitment*, 2010.

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### Mergers and acquisitions

A 2008 KPMG survey<sup>100</sup> revealed that cultural differences are a major post-deal issue, and companies frequently associate integration issues with cultural variation and complexity. Organisations should pre-empt these issues, as opposed to blaming cultural differences for difficulties experienced during post deal integration.

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 recent 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.

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.

### 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>101</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.

<sup>100</sup> KPMG, *All to Play For: Striving for Post Deal Success*, 2008

<sup>101</sup> CG Code Guideline 12.7

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Whistle-blowing 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>102</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 whistle-blowing policy should be disclosed in the company's annual report, and procedures for raising such concerns should be publicly disclosed as appropriate<sup>103</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/she has willfully made a false statement in their complaint. Similarly, Section 208 of the CA 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.

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.

<sup>102</sup> 20 Questions Directors Should Ask about Codes of Conduct, Gunns. M & Wexler, M. 2010

<sup>103</sup> CG Code Guideline 12.7

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# 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?
2. Is the Board sufficiently independent of management to enable it to make challenging decisions?
3. Is there a regular assessment of each director's independence made by the Board and is the process effective?
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?
5. Does the Board tailor its charter to the company's evolving operating environment and is the charter periodically reviewed?
6. Does the Board periodically review the Board's and Chairman's performance?
7. Are matters that must be referred to the Board for approval clearly communicated to management?
8. Are delegations to management, including the delegations policy documented?



## RED FLAGS

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

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

The Board's governance scope should include the following key functions<sup>104</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.

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

<sup>104</sup> CG Code Guideline 1.1

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- 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>105</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 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 AoA 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/her from exercising proper supervision and managerial control over the company. The CA S157(C) 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 makes proper inquiry.

The Board may also delegate authority to make decisions to any Board committee without relinquishing its responsibility<sup>106</sup>. Such delegation should be disclosed<sup>107</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>105</sup> CG Code Guideline 1.5

<sup>107</sup> CG Code Guideline 1.3

<sup>106</sup> CG Code Guideline 1.3

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## 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>108</sup>*

<sup>108</sup> <http://www.abc.net.au/news/2013-01-17/rio-tinto-ceo-to-step-down/4470040>, "Rio Tinto chief quits after heavy write-downs" and <http://www.smartcompany.com.au/leadership/29918-why-rio-tinto-gave-its-ceo-tom-albanese-a-push.html>,

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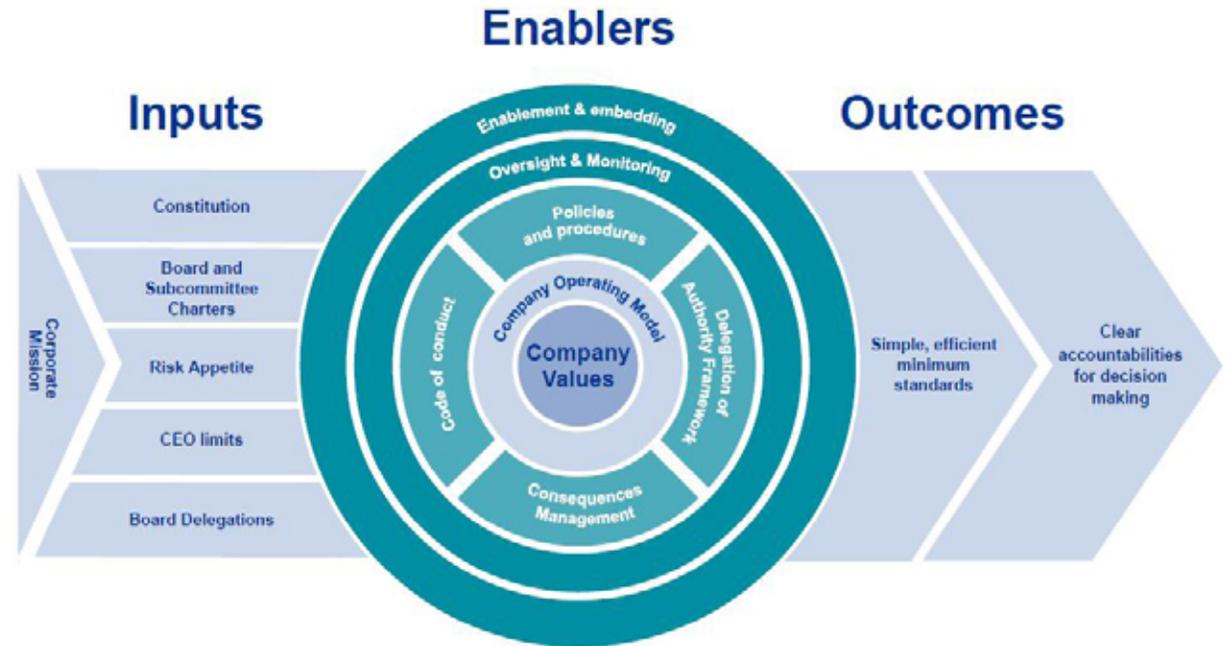
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### Accountabilities framework

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>109</sup>. As such, adequate steps should be taken to ensure compliance with legislative and regulatory requirements under the listing rules of securities exchange<sup>110</sup>.

The KPMG accountabilities framework below 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.

### KPMG accountabilities framework



<sup>109</sup> CG Code Principle 10 & Guideline 10.1

<sup>110</sup> CG Code Guideline 10.2

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### 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.

Commonly, non-executive directors have key responsibilities to deliver including<sup>111</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>112</sup>.

Additionally and according to the Higgs report<sup>113</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>114</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>115</sup>.

Independent directors should make up at least one-third of the Board<sup>116</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), he or she is part of the management team and is not independent<sup>117</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>118</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>119</sup>.

Each director's independence should be disclosed in the company's annual report<sup>120</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>121</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>111</sup> CG Code Guideline 2.7

<sup>112</sup> CG Code Guideline 2.8

<sup>113</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>114</sup> CG Code Guideline 2.3

<sup>115</sup> CG Code Principle 2

<sup>116</sup> CG Code Guideline 2.1

<sup>117</sup> CG Code Guideline 2.2

<sup>118</sup> CG Code Guideline 3.3

<sup>119</sup> CG Code Guideline 3.4

<sup>120</sup> CG Code Guideline 2.3

<sup>121</sup> CG Code Guideline 2.3 & 4.3

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- 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>122</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>123</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>124</sup>.

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

### 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.

<sup>122</sup>The Statement of Good Practice SGP No.7/2007

<sup>123</sup> CG Code Guideline 2.3 & 4.3

<sup>124</sup> CG Code Guideline 2.4

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### 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 AoA 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 CA allows a nominee director to divulge information of 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>125</sup>.
- The director is first authorised by the Board of directors to make the disclosure<sup>126</sup>.
- The disclosure will not be likely to prejudice the company<sup>127</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.

<sup>125</sup> CA Section 158(3)(a)

<sup>126</sup> CA Section 158(3)(b)

<sup>127</sup> CA Section 158(3)(c)

<sup>128</sup> CG Code Guideline 4.5

### 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 AoA 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.

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>128</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.

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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>129</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>130</sup>.

The responsibilities of the Chairman include<sup>131</sup>:

- Leading the Board to ensure its effectiveness on all aspects of its role
- Setting the agenda and ensure 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 common in Singapore for the Chairman to be the CEO as well since majority of the listed companies were historically family run businesses<sup>132</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.

<sup>129</sup> CG Code Principle 3

<sup>130</sup> CG Code Guideline 3.1

<sup>131</sup> CG Code Guideline 3.2

<sup>132</sup> Survey, NUS Business School Centre for the Governance, Institutions and Organisations, 2012

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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.

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>133</sup>.

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

- being available to shareholders where they have concern 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 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
- 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>134</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' stakeholders. The role has increasingly become more important and often time 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>135</sup>.

<sup>133</sup> CG Code Guideline 3.3

<sup>134</sup> CA Section 4(1)

<sup>135</sup> CG Code Guideline 6.3

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The Singapore Association of the Institute of Chartered Secretaries and Administrators (SAICSA)'s good governance guides provides 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:

- a. Advisor to the Board - advise and assists the Board with respect to their duties and responsibilities as directors, compliance with their obligations under the CA and SGX requirements and issues on corporate governance. Company secretary also act as a communication and information channel to executive, non-executive directors and management
- b. 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

- c. Corporate governance and compliance officer - ensure proper compliance with all relevant statutory and regulatory requirements
- d. Corporate communications - communicate with the stakeholders of the company as appropriate.

Additional principles to be applied to the company secretary role include<sup>136</sup>:

- Role should be clearly defined and should include the responsibility to ensure that all Board procedures are adhered to and compliance to 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>137</sup>.

<sup>136</sup> CG Code Guideline 6.3

<sup>137</sup> CG Code Guideline 6.4

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# 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?
2. Does the Board drive management to develop a business model that provides the organisation with a competitive advantage?
3. Are different strategic options considered prior to a final decision being made by the Board?
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?
5. For major projects, does management provide an in-depth business case which is independently verified?
6. Has the Board and management defined shareholder value and how it is measured?
7. Does the Board challenge and question management to achieve better strategy formulation?
8. Does management periodically provide the Board with performance benchmarks against the published figures of industry peers?
9. Are the strategic options presented by management based on robust and thorough analysis using established tools and methodologies?
10. Are post implementation reviews completed for all major projects?



## RED FLAGS

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

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### 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 sidelined 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.

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### 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)	

### 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.

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### Thinking strategically

A good corporate strategy presents a vision for the future and a roadmap for how the company will get there.

An effective, well-articulated, strategic plan is critical for organisational success.

Developing a strategy that presents a clear picture of where the company is heading 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.

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>138</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.

<sup>138</sup> CG Code Guideline 1.1(e)

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Boards must try to balance both short and longer-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 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.

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### 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.

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# 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?
2. Are there early warning systems in place to alert the Board and senior management to emerging risks?
3. Are the right risks being identified, assessed and managed?
4. Has the Board approved the risk appetite/ tolerance levels for the company?
5. Does the Board challenge the risk approach, risk reporting and management plans?
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

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

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### 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]
- Risk Governance Guidelines for Listed Boards (RGGLB).

### 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
	'Opinion of the Board, with the concurrence of the Audit Committee, on the adequacy of the internal controls, addressing financial, operational and compliance risks'	'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'
<b>Risk Management</b>		
Adequacy		✓
Effectiveness		✓
<b>Internal Controls</b>		
Adequacy	✓	✓
Effectiveness		✓

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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>139</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>140</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>141</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>142</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>143</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 otherwise should be established to assist the Board in carrying out its responsibility of overseeing the company's risk management framework and policies<sup>144</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>145</sup>.

Although it is not mandatory for listed companies in Singapore to comply with principles in the Code, SGX Listing Rule 710 mandates the requirements 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.

### 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, 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 Enterprise Risk Management (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.

<sup>139</sup> CG Code Principle 11

<sup>140</sup> CG Code Guideline 11.1

<sup>141</sup> CG Code Guideline 11.2

<sup>142</sup> CG Code Guideline 11.3

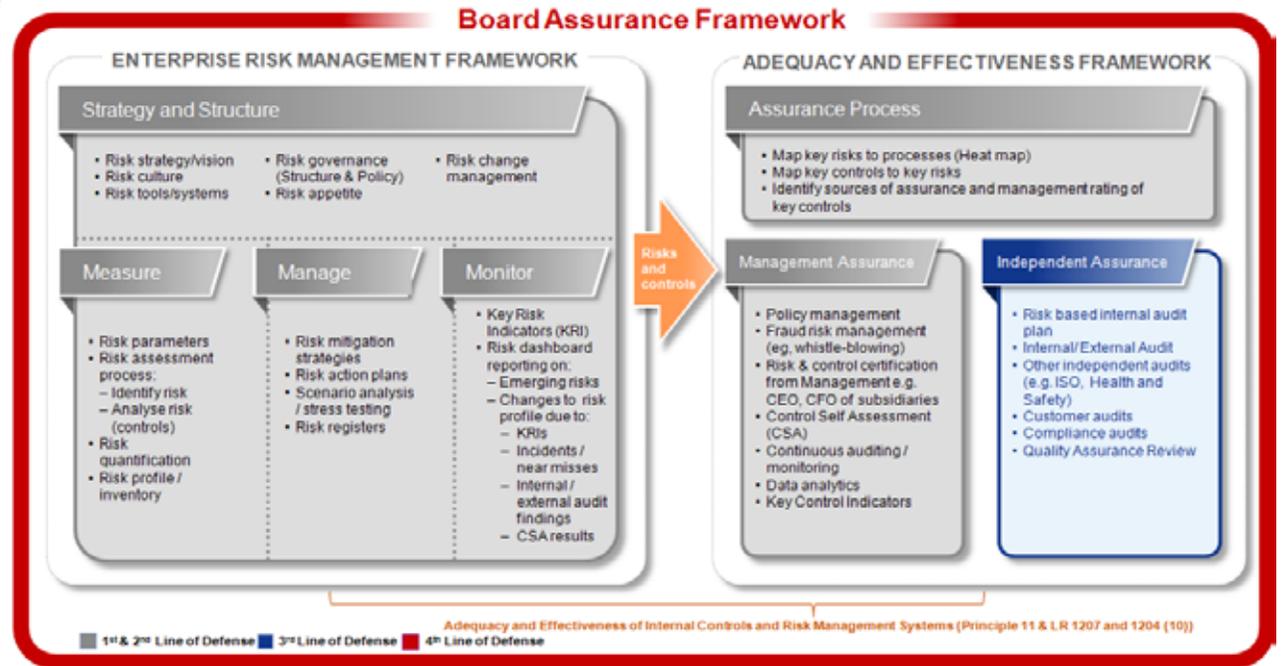
<sup>143</sup> CG Code Guideline 11.3

<sup>144</sup> CG Code Guideline 11.4

<sup>145</sup> SGX LR 1207 (10)

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Source: KPMG's Board Assurance Framework

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 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.

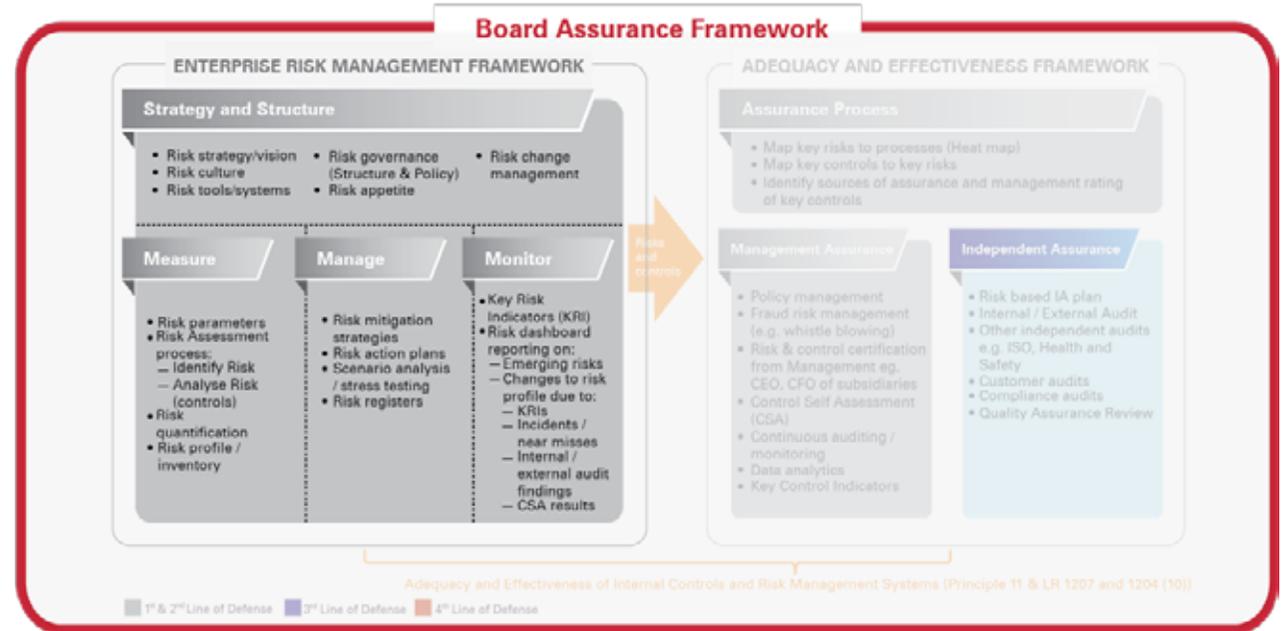
To satisfy the Board's accountability for risk governance, they should ensure there is an adequate and effective enterprise risk management system in place that is relevant for the nature, size, structure and complexity of their company.

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 RGGLB.

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



Source: KPMG's Board Assurance Framework

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.

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### Risk appetite

The Board should determine the company's levels of risk tolerance<sup>146</sup>. Risk appetite is the amount of risk, on a broad level, that an organisation is willing to accept in pursuit of value. 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>147</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.

### 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>148</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>149</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 RGGLB (page 9, Appendix A) where this is covered in more detail.

### 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>150</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 RGGLB for further information regarding risk management policies.

<sup>146</sup> CG Code Guideline 11.1

<sup>147</sup> RGGLB, Appendix D – "Setting Risk Tolerance"

<sup>148</sup> RGGLB, page 9

<sup>149</sup> Guidebook for ACs, page 60

<sup>150</sup> CG Code Guideline 11.1

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### 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.

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 RGGLB 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.

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### 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.

### Enterprise-wide risk management framework - process

Framework Element	Description
<b>Strategy and Structure</b>	
1. 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'
2. 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.
3. People & Culture	Educating and engaging people – Evaluating common and specific characteristics of risk culture to serve as an aiming point for ERM change programme.
4. 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>	
5. 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.
6. 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>	
7. Risk Monitoring & Reporting	Driving risk hindsight and foresight – Monitor and report significant risks from operations up to the Board.

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### 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.

#### *Risk management committee*

The Board may establish a separate Board risk committee to assist it in carrying out its responsibility of overseeing the company's risk management framework and policy<sup>151</sup>. A risk management committee 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>152</sup>), many companies have established risk management committees, 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 risk management committee.

Generally the risk management committee 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 Guidebook for ACs 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.

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'.

<sup>151</sup> CG Code Principle 11.4

<sup>152</sup> Financial institutions are required to establish a BRC under the Singapore FI CG Code

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### *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 Assurance for further information on the role of Internal Audit.

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



## RED FLAGS

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

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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>153</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>154</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<sup>155</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 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.

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.

<sup>153</sup> CG Code Guideline 1.3

<sup>154</sup> CG Code Guideline 2.6

<sup>155</sup> ISCA-KPMG 'Towards better risk governance' Study 2013

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### 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 result
- 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.

### Committee induction framework

Over the last 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 and regulations governing the areas impacting the company; where required, they should have access to seek independent advice from external consultants or advisors.

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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  
Meeting 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.

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>156</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>157</sup>.

<sup>156</sup> CG Code Guidelines 4.1, 7.1 & 12.1

<sup>157</sup> CG Code Guidelines 4.1 & 12.1

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### 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 to make 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>158</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>159</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
- 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 improvements
- 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.

<sup>158</sup> CG Code Principle 5

<sup>159</sup> CG Code Guideline 5.1

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### 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>160</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>161</sup>.

The NC is tasked to make recommendations to the Board on relevant matters<sup>162</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.

- 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.

<sup>160</sup> CG Code Guideline 4.1

<sup>161</sup> CG Code Guideline 4.1

<sup>162</sup> CG Code Guideline 4.2

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In order to put together and operate an effective NC, the following attributes are recommended to be in place<sup>163</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>164</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 AoA. 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
- 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 documentaton 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 been adequately carrying 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>165</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 resource 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>166</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.

<sup>163</sup> Nominating Committee Guide 2012 written by Associate Professor Mak Yuen Teen, of the NUS Business School together with Mr Irving Low, Partner and Head of Risk Consulting at KPMG Singapore

<sup>164</sup> CG Code Guideline 4.1

<sup>165</sup> CG Code Guideline 4.4 & 4.6

<sup>166</sup> CG Code Guideline 2.4

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### 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.

### 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

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### 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>167</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>168</sup>.

Similar to other Board committees, the RC should have proper terms of reference to include:

- Supporting the company in developing 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 provide 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>169</sup>

A key task of the remuneration committee 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.

<sup>167</sup> CG Code Principle 7

<sup>168</sup> CG Code Guideline 7.1

<sup>169</sup> CG Code Guideline 7.4

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### Audit Committee ("AC")

The Board is required to establish an AC with written terms of reference clearly setting out its authority and duties<sup>170</sup>.

Refer to Appendix 3 for a sample of an Audit and Risk Committee Charter.

### Composition of AC

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>171</sup>. At least two members, including the AC Chairman, should have recent and relevant accounting or related financial management expertise or experience<sup>172</sup>.

#### In 2013 KPMG surveyed 1,800 Audit Committee members in a number of countries.

The main opportunities for enhancing committee performance raised in this survey by many countries included:

Committees obtaining a deeper understanding of the key assumptions underlying management's material accounting judgements.

- Seeking greater value and insight from internal and external auditors.
- Audit Committees' self-evaluation process being robust and effective.

The Companies Act also requires the AC Chairman to be independent, with no involvement in any executive functions in the company or its related companies<sup>173</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>174</sup>.

#### In 2014 KPMG surveyed 1,500 Audit Committee members in a number of countries.

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.

<sup>170</sup> CG Code Principle 12

<sup>171</sup> CG Code Guideline 12.1

<sup>172</sup> CG Code Guideline 12.2

<sup>173</sup> CA Section 201B(3)

<sup>174</sup> CG Code Guideline 12.9

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The company is required to announce any appointment or reappointment of a director to the AC<sup>175</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>176</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 financials 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.

### Singapore Audit Committee Institute's Priorities for 2014<sup>177</sup>

- Keep abreast of regulatory change
- Balance the allocation of resources between compliance and performance
- Be aware of risks to the company's reputation
- Improve technology governance
- Embed a strong risk monitoring regime
- Elevate Internal Audit (IA) as a core independent assurance provider
- Stay focused on financial accounting and reporting
- Maintain strong ethics and integrity

<sup>175</sup> Listing Rule 704(8) / Catalyst Rule 704(7)

<sup>176</sup> Guidebook for ACs

<sup>177</sup> KPMG in Singapore: Adaptation of KPMG's Global Audit Committee Institute Survey 2014

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### 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.

### Risk Committee

Although not mandatory, many large organisations have established risk committees in recent years. Many are often combined with the AC. If a risk committee is established, its charter needs to be developed with reference to the intersection between its duties and those of other committees, particularly the AC.

Risk committees 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.

Refer to RGGLB for a sample of Board Risk Committee Charter.

The ultimate responsibility for risk oversight rests with the full Board, regardless of whether or not a separate risk committee is established.

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## 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, Mr. Leeson 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 that never existed in order to record profits in the reports that were sent to the head office in London. By the end of his game, which the management was completely unaware of for three full years, Leeson was sentenced to six and a half years jail after chalking up £827 million of losses which led to the bankruptcy of the bank.*

*This case highlights the importance of having a risk committee 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>178</sup>.*

<sup>178</sup> "Recent Cases on Corporate Governance in Singapore: The "Good", "Bad" and the "Ugly" by Tan Lay Hong (2009)

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### 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.

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# 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 and/or Audit Committee satisfied with the management's assurances on the company's risk management and internal control systems?
2. Does the Board receive regular independent assurance on the adequacy and effectiveness of the business risk management framework and controls?
3. Has an assurance map been developed that provides a consolidated view on who provides assurance across the organisation's key processes?
4. Does the external auditor test and challenge elements of the financial reporting, disclosure, risk and control environment?
5. Is the Board, through the Audit Committee, satisfied that the internal audit function is operating effectively and efficiently?
6. Is the internal audit plan clearly linked to the up-to-date risk profile?
7. Does the company have an effective and efficient integrated assurance framework – how do risk management activities integrate within the wider system of internal control?
8. Does the governance and assurance framework add value to the organisation?



## RED FLAGS

1. A compliance map does not exist to provide a gap analysis on assurance activities
2. The Board does not review the risk profile and internal audit plan on a periodic basis
3. Uncertainty exists over the processes supporting management attestations
4. 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
5. Internal audit projects are being cancelled or delayed by management
6. Recommendations made by assurance providers are not being tracked and implemented
7. The Audit Committee reports to the Board do not provide an overview of the internal audit work plan
8. There are significant accounting disagreements between management and the external auditor
9. The external auditor is not present when the Board considers the annual financial statements

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### What is assurance?

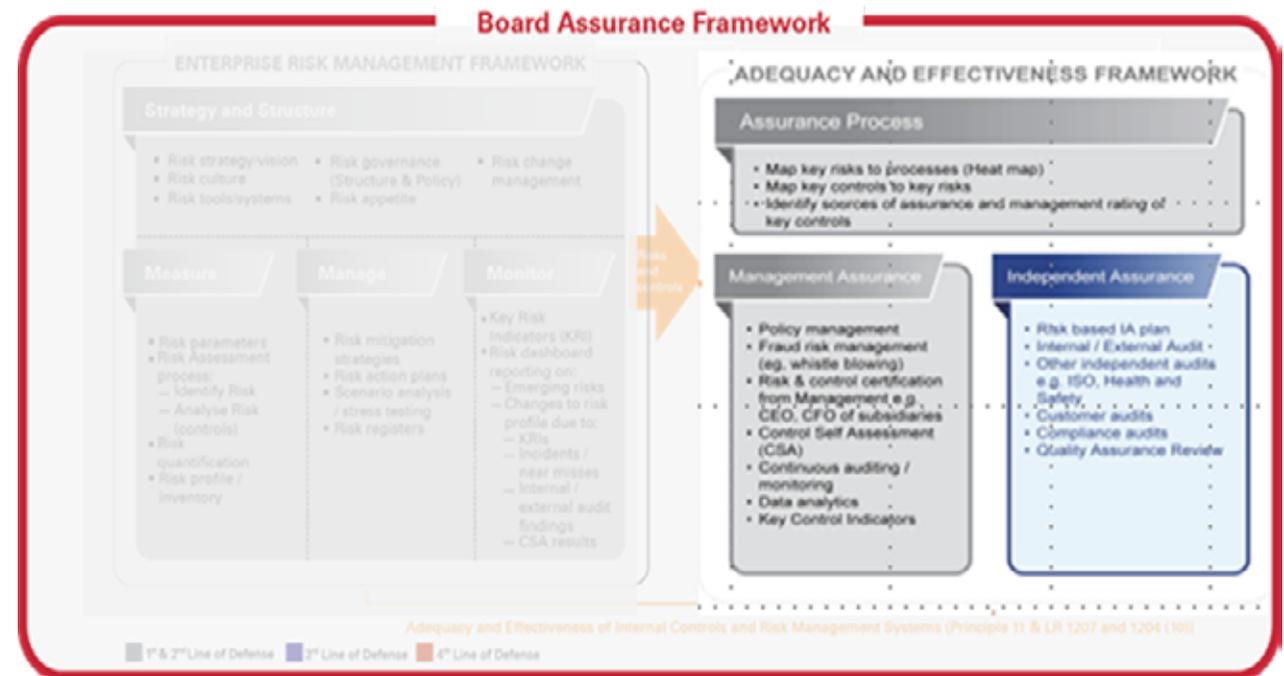
Assurance is an assessment process by which one can obtain a level of confidence over the matter at hand.

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 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.

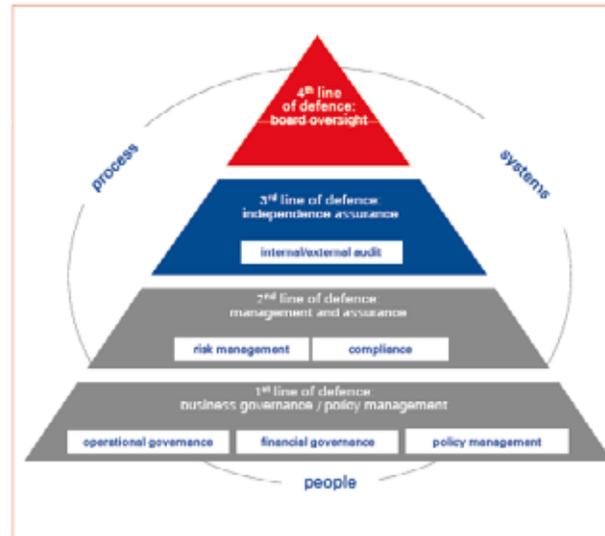
Companies should adopt a balanced mechanism in obtaining assurance from management, its oversight functions and independent assurance providers as highlighted in KPMG's four lines of defence model below. The model can be used to structure roles, responsibilities and accountabilities for decision making across governance, risk management and assurance activities.



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### 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 operations** – risk and control in the business

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.

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>179</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 system.

<sup>179</sup> CG Code Guideline 11.3

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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>180</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>181</sup>.

### 2. **Second line of defence: the oversight functions**

These are the groups which draft and implement policies and procedures and typically consist of people from the Human Resource, 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 7 for more details on the oversight function of Risk Management.

### 3. **Third line of defence: independent assurance providers**

#### **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>182</sup>.

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>183</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>184</sup>

<sup>180</sup> *Guidebook for ACs, page 77*

<sup>181</sup> *Guidebook for ACs, page 78*

<sup>182</sup> *CG Code Principle 13*

<sup>183</sup> *CG Code Guideline 12.4 (c)*

<sup>184</sup> *Guidebook for ACs, page 97*

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- 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>185</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 impact on the internal audit work, for example the changes in the CG Code, SGX LR and/or Companies Act<sup>186</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 auditable units in terms of timing, 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.

- 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.

<sup>185</sup> CG Code Guideline 13.2, 13.3 & 13.5

<sup>186</sup> CG Code Guideline 12.8

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### 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 comply with give a true and fair view of its financial position<sup>187</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>188</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>189</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
- 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

<sup>187</sup> CA S201(3) & S207

<sup>188</sup> SGX LR / Catalyst Rule 712(2)

<sup>189</sup> SGX LR / Catalyst 713(1)

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### Sustainability reporting

Sustainability reporting is not a mandatory requirement for Singapore listed companies. But globally, there is increased interest in sustainability issues, including the economic, environmental and social impact a company has on its community. Assurance on a sustainability report increases stakeholders' confidence in the accuracy and completeness of the information as well as adds credibility to the report. It is also an important feedback mechanism to listed companies in improving the quality of their sustainability reports.

SGX encourages companies to disclose its sustainability policy, including mitigation of risks, performance data and other material information which will provide the stakeholders' deeper understanding of corporate performance. Sustainability reporting complements financial disclosure to give a comprehensive account of how the company has performed. Companies should provide a balanced and objective view of their performances by including both positive and negative impacts.

Listed companies may engage external assurance providers to conduct independent verification of the sustainability reports<sup>190</sup>.

### 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 are planning 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.

<sup>190</sup> *Guide to Sustainability Reporting for Listed Companies, 2011*

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### 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).

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 (in relation to SGX LR 1207(10) requirements)	Example disclosures
<b>Clean opinion</b>	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].
<b>Adverse opinion</b>	<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.

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# 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?
2. Is there potential for the company to improve investor confidence by meeting stricter corporate governance standards of markets it is not listed in?
3. What are current shareholders expectations of corporate governance?
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?
6. Is management kept abreast of changes in corporate governance standards?
7. Is management aware of the corporate governance expectations of some of the larger institutional investors?
8. Is management aware of the diversity of corporate governance standards across different jurisdictions?



## RED FLAGS

1. The company is dual-listed or multi-listed, but only follows the governance code of their primary listing
2. No member of the Board is accountable for keeping up to date with corporate governance requirements and legislation
3. Corporate governance rarely features on Board meeting agendas
4. Accountability for maintenance of the Board instruments is not clear
5. The company's annual report does not include all disclosures required by corporate governance legislation
6. Directors are unfamiliar with best practice standards for corporate governance and risk management

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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) Principle 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. The entire *OECD Principles of Corporate Governance* can be found at <http://www.oecd.org/dataoecd/32/18/31557724.pdf>

#### SUMMARY OF OECD PRINCIPLES

Ensuring the basis for an effective corporate governance framework

The corporate governance framework should promote transparent and efficient markets, be consistent with the rule of law and clearly articulate the division of responsibilities among different supervisory, regulatory and enforcement authorities.

The rights of shareholders and key ownership functions

The corporate governance framework should protect and facilitate the exercise of shareholders' rights.

The equitable treatment of shareholders

The corporate governance framework should 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.

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 cooperation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises.

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### SUMMARY OF OECD PRINCIPLES

#### 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.

#### Singapore

*The SGX Corporate Governance Principles and Recommendations*

The SGX Corporate Governance Council's Corporate Governance Principles and Recommendations (SGX Principles) provide a set of corporate governance 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 conform, to disclose that fact and the reasons why.

The SGX Corporate Governance Council revised the SGX Principles which was released on the 1st of 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 was 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/>

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### *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 effectiveness of internal control over financial reporting. As a result, auditors evaluate and test a company's internal control in a different light and in greater depth. The overall goal of SOX compliance is to strengthen internal control 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 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/dodd-frank.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.

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### 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.

#### *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.

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### 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 Organization for Standardization. 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.

### Superannuation

The Central Provident (CPF) was established by the Central Provident Fund Act (Chapter 36, 1999 Revised Ed) in 1955 ("CPF Act"). It is a comprehensive social security savings system that provides Singaporean members with financial security in old age by requiring a minimum retirement sum to be preserved. In addition, it covers the needs of families in healthcare, home ownership, family protection and asset enhancement for its members.

### Health

Healthcare in Singapore is mainly under the responsibility of the Singapore Government's Ministry of Health (MOH). Singapore's system uses a combination of compulsory savings from payroll deductions to provide subsidies within a nationalised health insurance plan known as Medisave.

### Pharmaceutical

Under the Medicine Act (Chapter 176, 1985 Revised Ed) in 1977, all western medicines are subject to product registration prior to their sale and supply in Singapore. The safety, quality and efficacy of western medicines are scientifically assessed by the Health Sciences Authority (HSA) to meet internationally benchmarked standards before marketing approval is granted. All local manufacturing facilities engaged in the manufacture or assembly of medicinal products and Chinese Proprietary Medicines (CPM) must be licensed with HSA. The manufacturers are expected to comply with the relevant legislative and regulatory requirements, and Good Manufacturing Practice (GMP) standards.

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# 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?
2. Does the Board receive regular briefings from the company's investor relations officer?
3. Do the Chairman and directors play an active role in the investor relations program?
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?
6. Does the Board have a process to ensure that all statutory reporting obligations are met in a timely manner?
7. Is there a continuous disclosure policy approved by the Board and linked to the spokesperson policy?
8. Does the Board regularly review the effectiveness of its business reporting and communication in assisting investor decision-making?



## RED FLAGS

1. Major marketplace concern regarding executive remuneration incentives
2. The AGM is a major public relations challenge
3. The investor relations manager has no contact with the Board
4. There is no strategy of how to handle private equity approaches
5. Institutional investors publicly voice concerns regarding some of the organisation's governance practices
6. The SGX expresses concern regarding the timeliness of the organisation's market disclosures
7. The linkage between financial and non-financial reporting is not evident in external communications
8. There is significant protest vote against the company's remuneration report

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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>191</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 AoA or similar governing document
- Nominating and appointing directors
- Receiving continuous disclosure of material developments in the company's affairs<sup>192</sup>
- Calling a general meeting of shareholders, and/or proposing a resolution to be considered at a general meeting
- Voting at the AGM<sup>193</sup>
- Obtaining an independent valuation of their securities
- Inspecting the minute books for members' meetings
- Suing the corporation for wrongful acts
- Allowing corporations which provide nominee or custodial services to appoint more than two proxies<sup>194</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 AoA 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 AoA to allow for absentia voting at general meetings of shareholders<sup>195</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>196</sup>. Companies with an effective approach to investor relations will understand the objectives of different investor groups and key individual investors. Communication and active engagement with shareholders generates feedback on investor concerns.

<sup>191</sup> CG Code Principle 14

<sup>192</sup> CG Code Guideline 14.1

<sup>193</sup> CG Code Guideline 14.2

<sup>194</sup> CG Code Guideline 14.3

<sup>195</sup> CG Code Guideline 16.1

<sup>196</sup> CG Code Principle 15

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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>197</sup> and approve any policies that control investor relations engagement risks. The Board should 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>198</sup>.

Regular dialogues with shareholders to gather feedback and address shareholders' concerns should also be established and maintained<sup>199</sup>. Such engagements with the shareholders should be stated in the company's annual report<sup>200</sup>.

Companies are also encouraged to have a policy on payment of dividends and should communicate it to shareholders<sup>201</sup>.

### Institutional shareholders' role in governance

Several sets of best practice principles have been published addressing the responsibilities of institutional investors. One such example includes the International Corporate Governance Network's (ICGN) Statement of *Principles on Institutional Shareholder Responsibilities*<sup>202</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

<sup>197</sup> CG Code Guideline 15.1

<sup>198</sup> CG Code Guideline 15.2

<sup>199</sup> CG Code Guideline 15.3

<sup>200</sup> CG Code Guideline 15.4

<sup>201</sup> CG Code Guideline 15.5

<sup>202</sup> 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).

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- 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 reports must be sent to the members not less than 14 days before the AGM<sup>203</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 your company's AoA. The minimum period of notice is 14 days, though the AoA may provide for a longer period of notice<sup>204</sup>. The notice period can, however, be shortened if all members of your company who are entitled to attend and vote at the AGM agree to it<sup>205</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>206</sup>.

Notices may be served personally, by post, e-mail and other forms of electronic communication<sup>207</sup> or any other means permitted by the company's AoA.

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>208</sup>.

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; and

<sup>203</sup> CA Section 203(1)

<sup>204</sup> CA Section 177(2)

<sup>205</sup> CA Section 177(3)

<sup>206</sup> CA Section 185

<sup>207</sup> CA Section 387A & 387B

<sup>208</sup> CA Section 183

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2. A written notice of the special resolution has been given to shareholders at least 21 days' in advance (for listed companies)<sup>209</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 one month after its passing<sup>210</sup>. Other than that, an ordinary resolution to allot shares is also required to be lodged<sup>211</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/her at the meeting<sup>212</sup>. The proxy does not necessarily have to be a shareholder.

### 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>213</sup>.

AGMs are governed by the CA (Section 174 to Section 176), the company's AoA 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>214</sup>.

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

<sup>209</sup> CA Section 184(1)(b)

<sup>210</sup> CA Section 186

<sup>211</sup> CA Section 161(5) & 186

<sup>212</sup> CA Section 181

<sup>213</sup> CG Code Principle 16

<sup>214</sup> CG Code Guideline 16.3

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- 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>215</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>216</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>217</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>218</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>219</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 Singapore Accounting Standard
- SGX LR
- Singapore Code of Corporate Governance (non-statutory).

The key elements of the statutory reporting portfolio for listed companies include:

- A quarterly, half-yearly and full year reporting
- An annual audited financial report and directors' statement and report
- Corporate Governance Statement<sup>220</sup>
- 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

<sup>215</sup> CA Section 176

<sup>216</sup> CG Code Guideline 16.2

<sup>217</sup> CG Code Guideline 16.5

<sup>218</sup> CG Code Guideline 16.4

<sup>219</sup> *Rethinking Board and Shareholder Engagement in 2008*, By Weil, Gotshal & Manges LLP

<sup>220</sup> SGX LR 710

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- 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 applicable legislation applicable to the 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' report
- 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' report

The directors must prepare a directors' report made in accordance with a resolution of the directors, which is signed by at least two directors<sup>221</sup>. The directors' report requirements are set out as per the requirements of the CA. The required reporting obligations will vary for companies which are listed, limited by guarantee, large proprietary and listed or unlisted registered schemes.

The minimum requirements of the annual directors' report are set out in section 201 of the CA. Additional information that is required to be included in the annual report is also specified in SGX LR 1207.

<sup>221</sup> CA Section 201(6)(a) & 201(15)

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### 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.

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<sup>222</sup>.

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>223</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>224</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.

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

<sup>222</sup> CA Section 201(15)(c)

<sup>223</sup> CA Section 207(2)(b)

<sup>224</sup> SGX LR 710

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- 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>225</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 and directors' 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 Board 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 result 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)
- The assurance provided by the CEO and CFO<sup>226</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.

<sup>225</sup> CA Section 203A

<sup>226</sup> CG Code Guideline 11.3

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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.

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.

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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).

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# 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?
2. Have stakeholders with the ability to affect strategic and business objectives been engaged effectively?
3. Have the risks of not engaging key stakeholders (financial and reputational) been considered and, if applicable, quantified?
4. Is stakeholder engagement embedded into the company's vision, mission and strategy statements?
5. Does the company have a stakeholder engagement framework aligned with best practice?
6. Do relationship effectiveness measures exist for key stakeholders?
7. Is the Board seeking and maintaining relationships with its key stakeholders at the leadership level?
8. Has the company considered making a public disclosure about stakeholder management and corporate social responsibility?
9. Is effective stakeholder management used as a strategic, preventive mechanism, rather than a responsive tool?



## RED FLAGS

1. The company maintains no stakeholder mapping, tiering or profiling information
2. Stakeholders are defined narrowly as clients and customers
3. In most decisions, stakeholders are not considered or consulted
4. The risk of not engaging stakeholders is not discussed or is often dismissed quickly by some Board members
5. Dialogue with stakeholders mostly occurs in the event of disputes and negative media coverage
6. Online coverage of the company is mostly negative

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### Stakeholder engagement

The Board's role is to ensure that obligations to shareholders and other stakeholders are understood and met<sup>227</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.

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>228</sup>.

<sup>227</sup> CG Code Guideline 1.1(e)

<sup>228</sup> For further information please refer to *AA1000 Stakeholder Engagement Standard* <http://www.accountability.org/images/content/3/6/362/AA1000SES%202010%20PRINT.pdf>

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### 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.

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.

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.

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### Increasing trend of sustainability reporting

The business biosphere, for many companies, is no longer about reaching the bare minimum in adhering to laws and regulations, but there is an emphatic shift in achieving and exceeding stakeholder expectations. To put this into perspective, 95 percent of the 250 world's largest companies publish sustainability reports<sup>229</sup>.

In Singapore, sustainability reporting remains voluntary – there is no legislative requirement for companies to publish such reports, although some companies may, for example, be required to prepare specific environmental reports to achieve compliance with particular legislation. SGX encourages all listed companies to consider sustainability reporting as an integral part of good corporate governance. Sustainability reporting is particularly relevant for listed companies which:

- Operate in industries that are susceptible to environmental and social risks;
- Operate in industries that produce significant environmental pollutants;
- Are heavy users of natural resources
- Are part of a supply chain where end customers demand that suppliers and contractors behave responsibly.

Specifically, listed companies which are operating in the following high-impact sectors should set the tone and undertake sustainability reporting<sup>230</sup>:

- Agriculture
- Air transport
- Chemicals and pharmaceuticals
- Construction
- Food and beverages
- Forestry and paper
- Mining and metals

- Oil and gas
- Shipping
- Water.

Companies should understand and respond to key trends and developments that affect sustainability reporting, including:

- Developing more concise sustainability reports
- Expanding reporting boundaries to include value chain considerations and spheres of influence
- Developing innovative reporting strategies that are more responsive to stakeholder needs
- Placing an increased focus on communicating sustainability opportunities that a company may seek to explore.

### Components of an effective sustainability response

The relative importance of particular sustainability-related risks and opportunities varies significantly between industry sectors and between companies within particular sectors. However, there is commonality in the key components of what may be described as an 'effective sustainability response'.

These components are primarily concerned with the management team's ability to:

- Understand broad sustainability-related concepts and issues, particularly those of potential relevance to their industry sector/company
- Establish effective stakeholder engagement processes
- Identify and appropriately prioritise sustainability-related risks and opportunities (often using a documented framework that seeks to consider the relative materiality of particular issues)

<sup>229</sup> KPMG International Survey of Corporate Responsibility Reporting, 2011

<sup>230</sup> Guide to Sustainability Reporting for Listed Companies, 2011

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- Develop an appropriate sustainability strategy (and associated vision/objectives)
- Communicate the developed sustainability strategy
- Execute the agreed strategy and integrate this within mainstream business activities
- Establish appropriate performance indicators and track progress (performance against target)
- Distribute sustainability performance information to key stakeholder groups (e.g. through a formalised sustainability report)
- Establish feedback/review mechanisms to monitor the effectiveness of sustainability-related activities and modify the underlying strategy in light of this feedback.

### 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 – G8 makes 'the 3Ts: Taxes, Transparency & Trade' the theme of the 39<sup>th</sup> G8 summit (June 2013)

As a result of reports of various multinational companies engaging in complex international tax and transfer pricing arrangements, UK Prime Minister and host of the 39<sup>th</sup> G8 Summit, David Cameron, declared that the agenda would focus on "trade, transparency and tax". The announcement of the agenda items coincides with recent showings of public discontent over the tax arrangements of multinational corporations and statements by various governments around the world announcing their intentions to further investigate the tax schemes of global companies  
Source: Cameron announces that G8 will focus on 3Ts: Taxes, Transparency and Trade <http://www.forbes.com/sites/kellyphilipserb/2013/06/17/cameron-announces-that-g8-will-focus-on-3ts-taxes-transparency-trade>

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# 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?
2. Do we understand the potential personal financial upside to management from a PE deal?
3. Are protocols in place to secure independent review of any approach?
4. Do we need to set up an independent sub-committee to lead decision-making and process-manage a potential transaction?
5. Does the Board understand the position of key shareholders?
6. Should a broader sale process be initiated to maximise shareholder value?
7. Is the Board clear on its requirements regarding when and what to disclose to the markets?
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?
9. Does the Board discuss the approach or the proposed transaction in closed sessions without participating directors and management?
10. What will the impact of the PE approach have on the Board's normal agenda?



## RED FLAGS

1. The Board has in the past been caught unaware by PE bids
2. No strategy has been developed for dealing with PE bids and it is rarely discussed at Board meetings
3. Continuous disclosure issues have been raised against the company over past PE bids
4. Directors' messages are inconsistent or unclear regarding their position on PE bids
5. Independent advisers are usually not engaged to examine PE submissions

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### 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

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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>231</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, Company Secretary 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.

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# 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?
2. Do we have the support, resourcing and experience we need to deliver?
3. Are there clear priorities on what needs to be looked into first?
4. Are we aligning our frameworks, policies and appointments with our strategy?
5. Is the Board defining its 'risk appetite'?
6. Do we have access to better practice frameworks and instruments?



## RED FLAGS

1. There is no consensus on the initial priorities
2. There is limited understanding on what is required in the establishment phase
3. The Board comprises mainly inexperienced directors
4. No advice is being sought from experts or directors who have experience in establishing a new Board
5. No time has been planned for discussing alignment with 'risk appetite' and strategy
6. There is no clear establishment and documentation of accountabilities and delegations
7. No Board instruments have been presented for review and approval

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### 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.

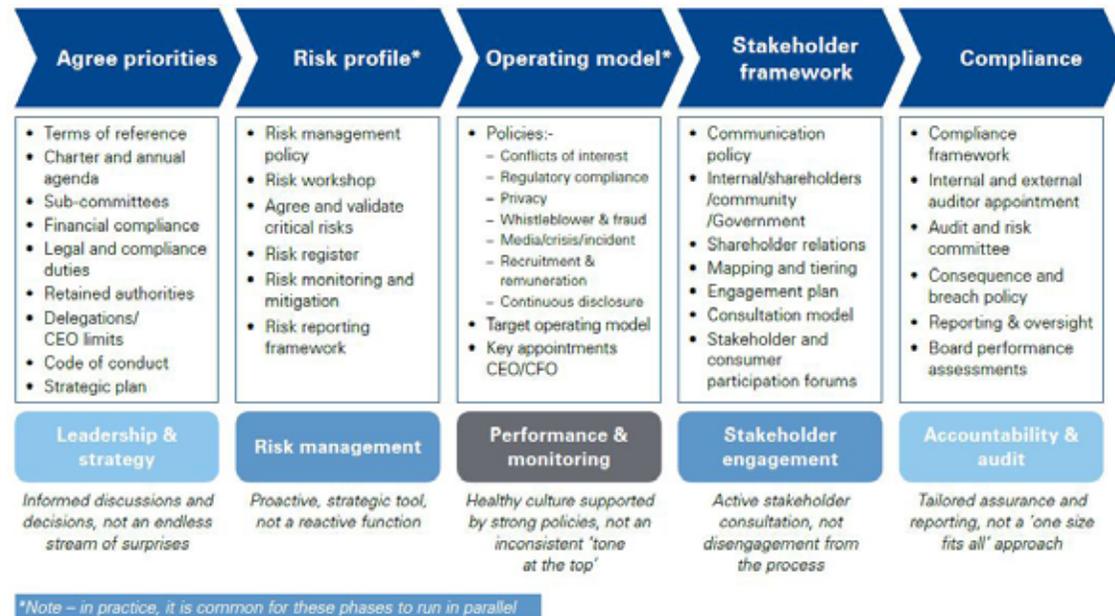
The framework begins by establishing a direction and clear set of priorities for the newly established Board. During this stage, the Board should document its plan and establish timelines and accountabilities around achieving its milestones.

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.



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# 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.

## Board Charter

Adopted on [date of adoption]

### 1 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. This Charter explains the Company's commitment to corporate governance.

### 2 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 oversees management's control and accountability framework. The Board is ultimately accountable to the Company's shareholders for the performance of the business.

### 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-making process through their technical expertise and knowledge of the business and its industry.

<sup>231</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)

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- A non-executive director is not employed by the Company, but in a management position of the Company. 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.

## 3 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 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 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.

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### 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.

### 4 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.

### 5 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.

### 6 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
- 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.

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### *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.

### **7 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.

### **8 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.

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## 9 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.

## 10 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.

## 11 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.

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# 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 5 (example Audit Committee and annual agenda).

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EXAMPLE BOARD ANNUAL AGENDA WORK PLAN

	Reserved authorities	Delegated authorities	Reporting	Matters that may be applicable to all meetings	
Meeting 1	<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>	
Meeting 2	<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>Audit committee report</li> <li>CEO/CFO report</li> <li>Major project reports</li> <li>Risk management report</li> </ul>		
Meeting 3	<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>		
Meeting 4	<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>OH&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>		<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>
Meeting 5	<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>		
Meeting 6	<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>Nominations committee report</li> <li>CEO/CFO report</li> </ul>		
Meeting 7	<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>		

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EXAMPLE BOARD ANNUAL AGENDA WORK PLAN

	Reserved authorities	Delegated authorities	Reporting	Matters that may be applicable to all meetings
Meeting 8	<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>Whistleblower report</li> <li>CEO/CFO report</li> <li>Major project reports</li> <li>Risk management report</li> <li>External audit report</li> </ul>	
Meeting 9	<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' report, 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>	
Meeting 10	<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>	<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>
Meeting 11	<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 project reports</li> <li>Risk management report</li> <li>Analyst and institutional presentations</li> </ul>	
Meeting 12 Board/management strategy day	<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>	

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# Appendix 3: Sample Audit and Risk Committee Charter<sup>232</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, and information technology controls)
- Internal audit (resources, performance and scope of work)
- External audit (qualifications, independence, engagement and fees).

Additional delegation of responsibilities to the Audit and Risk Committee (ARC) may include the following:

- Compliance (legal, regulatory and company policies)
- Interested persons transactions (IPTs).

## Authority

The ARC is authorised<sup>233</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>234</sup>.

## Membership

The Board shall appoint an ARC that has sufficient and relevant expertise to fulfill its role effectively<sup>235</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>236</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>237</sup>.

## Secretary

The Secretary of the company shall be the Secretary of the ARC.

<sup>232</sup> Guidebook for ACs, Appendix A2

<sup>233</sup> CG Code Guideline 12.3

<sup>234</sup> CG Code Guideline 6.5

<sup>235</sup> CG Code Guideline 12.2

<sup>236</sup> CG Code Guideline 12.1

<sup>237</sup> CG Code Guideline 12.8

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### 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 tele- 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>238</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>239</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>240</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 fulfill its role effectively<sup>241</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
- 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>242</sup>.

<sup>238</sup> CG Code Guideline 12.5

<sup>239</sup> CG Code Principle 5

<sup>240</sup> CG Code Principle 5

<sup>241</sup> CG Code Guideline 12.2

<sup>242</sup> CG Code Guideline 11.3

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### 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>243</sup>
- Review the company's risk profile/risk dashboard on a regular basis to understand the significant risks 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, operational, compliance and information technology controls<sup>244</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>245</sup>
- 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 and internal control systems<sup>246</sup>
- Review the company's procedures for detecting fraud and whistle-blowing, 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>247</sup>

<sup>243</sup> CG Code Guideline 11.1

<sup>244</sup> CG Code Guideline 11.2

<sup>245</sup> CG Code Guideline 11.3

<sup>246</sup> CG Code Guideline 11.3

<sup>247</sup> CG Code Guideline 12.7

<sup>248</sup> CG Code Guideline 12.4

<sup>249</sup> CG Code Guideline 13.5

<sup>250</sup> CG Code Guideline 13.1

### iii) Overseeing Internal Audit

- Monitor and assess the role and effectiveness of the IA function<sup>248</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>249</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>250</sup>
- Participate in the appointment, replacement or dismissal of the Head of IA<sup>251</sup>.

### iv) Overseeing External Audit

- Oversee the company's relations with the external auditor (including audit scope, approach and fees)<sup>252</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>253</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>254</sup>

<sup>251</sup> CG Code Guideline 13.1

<sup>252</sup> CG Code Guideline 12.4

<sup>253</sup> CG Code Guideline 12.4

<sup>254</sup> CG Code Guideline 12.6

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- 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.

### 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.

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# 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.

Assessing Financial Year End 31 December	Scheduled meetings			
	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) - 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 whistle-blowing 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				

 Recommended timing  
 As required

Source: Guidebook for ACs, Appendix B1