

Shining more light on non-ED remuneration

All emoluments paid to non-executive directors should also require shareholder approval. **BY MAK YUEN TEEN**

NON-EXECUTIVE director (NED) remuneration often receives little attention from investors because their amounts generally do not make much of a dent on the profits of a company. However, poorly conceived NED remuneration schemes can compromise the independence of independent directors (IDs). Some codes of corporate governance recommend that NEDs be remunerated differently from executive directors (EDs) and highlight that how NEDs are remunerated may be relevant in assessing their independence. The UK Code specifies that NED remuneration should not include share options or performance-related elements, and that holding of share options could be relevant to the determination of director independence.

In Singapore, many companies still disclose individual NED remuneration in meaningless bands of "below S\$250,000", even though the Code recommends disclosure of the exact remuneration. Tenuous reasons for not disclosing fully the remuneration of EDs and key executives, such as fear of poaching or loss of competitive advantage, are even less convincing in the case of NEDs. Further, as the examples below show, what makes up NED remuneration, how it is determined, and the amounts put to shareholders for approval are often unclear or questionable.

Last year, Chew Yi Hong and I wrote about Natural Cool Holdings (*"Burning issues at Natural Cool Holdings"*, BT, June 24). We questioned the ex-gratia payment equivalent to three years of director fees to the three IDs "as a token of appreciation and recognition of their contribution in the past years rendered to the company and/or its subsidiaries as independent directors". The IDs had been involved in what we felt were contentious decisions made by the company. These included acquiring and then proposing to dispose of a paint business after just eight months through an interested person transaction (IPT) which involves the company taking a hair-cut on an inter-company loan – although the IPT was subsequently aborted.

BONUSES FOR INDEPENDENT DIRECTORS

At Catalyst-listed GKE Corporation, the three IDs were paid "bonuses" of 16-17 per cent of their individual remuneration for FY2016, while the NED received a 20 per cent "bonus". Two of the IDs were newly appointed on Sept 30, 2015, replacing two others who resigned on the same day. It was the first time that the company had paid "bonuses" to IDs and NEDs.

GKE did not say how the bonuses were determined, which led SIAS to question their rationale. SIAS also questioned the significantly higher remuneration paid to the two EDs, with large bonus components, given that the core business was only just profitable and that losses were reported for the previous two years.

Payment of "bonuses", without explaining their basis, raises concerns of a possible breach of the listing rules or articles. Appendix 4C, rule 9(c) of the Catalyst rulebook states that the articles should include the following provision: "Fees payable to non-executive directors shall be by a fixed sum, and not by a commission on or a percentage of profits or turnover.

Salaries payable to executive directors may not include a commission on or a percentage of turnover."

The same rule applies to Mainboard companies. But it may be confusing because while a bonus is strictly not a "fixed sum", a liberal interpretation may suggest that it is acceptable to pay NEDs (including IDs) bonuses, provided they are not based on "commission on or a percentage of profits or turnover". For example, IDs may be paid bonuses tied to the company achieving business targets other than profits or turnover. This would nevertheless be questionable from a governance perspective and may affect the independent judgement of directors.

The sponsor clarified with me that the "bonus" was "an additional fee for the Independent Directors to recompense them for additional time and effort spent in advising and guiding the Group in a few transactions that had occurred last year ... The fee was proposed by management without any prior knowledge of the IDs, and the quantum was fixed and not based on any formula nor financial measures".

Comparing the latest year with the previous year, there was no increase in number of board or committee meetings, although this is not to say that the NEDs may not have spent more time. However, it is highly unusual to call such additional fees "bonuses". Further, since the IDs serving on the remuneration committee approved increased remuneration for the EDs while the EDs proposed additional "bonuses" to the IDs, there is an obvious perception problem.

Further, in its directors' remuneration table in the corporate governance report, GKE stated that only the directors' fees,

It would be illogical to require only certain types of NED remuneration to be approved by shareholders because it may lead companies to load up on components that do not require approval.

and not the bonuses paid to the IDs, were subject to the approval of shareholders. The sponsor has clarified, however, that this was an error and that the "bonuses" were included in the amount put up to shareholders for approval. All this ambiguity could have been avoided if GKE had been more transparent.

At Vicplas International, it was disclosed that "other benefits" were paid to its independent chairman and one of the NEDs, amounting to 53 per cent and 40 per cent of their remuneration respectively. These "other benefits" for NEDs started appearing in the directors' remuneration report from FY2012. The company did not disclose what these "other benefits" were – an analysis of its annual reports suggests that they were probably (largely) the fair value amounts of vested share options. While the Singapore Code is silent on the use of share options for NEDs, as mentioned earlier, some other codes do caution about their use especially for IDs.



ILLUSTRATION: MAK YUEN TEEN, CHRIS BENNETT

Vicplas did not appear to have put the actual number or value of share options granted to NEDs to shareholders for approval, although it did seek shareholders' approval to grant options pursuant to its share option plan, disclose that NEDs are entitled to participate in the plan, and disclose the number of options granted to NEDs in the directors' report.

At Stratch Group, three IDs and one NED were granted about two million options, but the company disclosed that it did not include the value of these options in the directors' remuneration table. Guideline 9.2 of the Code clearly states that in disclosing the remuneration of each director, "there should be a breakdown (in percentage or dollar terms) of each director's and the CEO's remuneration earned through base/fixed salary, variable or performance-related income/-bonuses, benefits in kind, stock options granted, share-based incentives and awards, and other long-term incentives".

Again, it also appears that the actual number or value of options granted was not included in the amount put to shareholders for approval.

Section 169 of the Companies Act states: "A company shall not at any meeting or otherwise provide emoluments or improve emoluments for a director of a company in respect of his office as

such unless the provision is approved by a resolution that is not related to other matters and any resolution passed in breach of this section shall be void."

It defines "emoluments" as including "fees and percentages, any sums paid by way of expenses allowance in so far as those sums are charged to income tax in Singapore, any contribution paid in respect of a director under any pension scheme and any benefits received by him otherwise than in cash in respect of his services as director".

Clearly, it would be illogical to require only certain types of NED remuneration to be approved by shareholders because it may lead companies to load up on components that do not require approval.

I have pointed out that many companies did indeed interpret "emoluments" as "cash fees" and do not put up all components of NED remuneration for shareholder approval. The examples discussed above, and many more that I am aware of, show that many companies continue to inter-

pret section 169 to only require the actual or maximum amount of cash fees paid to directors to be approved by shareholders.

Companies that wish to use share-based remuneration for NEDs should take a leaf from others such as Yoma Strategic Holdings. At Yoma's AGM on July 26, 2016, the company sought approval from shareholders to pay total directors' fees of up to S\$380,000 and 150,000 remuneration shares for each of the four independent directors for the financial year ending March 31, 2017.

FEES FOR SUBSIDIARY BOARDS

In Stratch's case, it also disclosed that, going forward, NEDs who serve on the group's direct and indirect subsidiaries (except one) would be paid separate fees at 90 per cent of the annual NED fees of the company. It disclosed eight direct and indirect subsidiaries, including five dormant ones and one for which it specifically stated that no additional fees will be paid – presumably, additional fees will be paid for two "active" subsidiaries.

Stratch's decision raises an issue that may also apply to other companies. If a listed issuer pays separate fees to NEDs for serving on other boards in the group, are companies expected to disclose such fees in the directors' remuneration report? Some issuers appear to interpret the guidelines to refer to fees for the "company" only, rather than for the group.

Similarly, as section 169 refers to "the company", fees paid to NEDs for serving on subsidiaries may not be included in the amounts put to shareholders of the listed company for approval.

A check with some company secretaries indicates different viewpoints. While it was not common for NEDs to sit on boards of unlisted subsidiaries or to be paid separate fees for doing so, one view was that the remuneration table excludes fees paid for serving on subsidiary boards, while another was that the remuneration table and the amount put to shareholders for approval should be on a group basis.

NEDs should be remunerated fairly for their time, responsibilities and contributions. However, remuneration should be appropriate and transparent. Issuers should disclose all remuneration paid to NEDs, including those paid for serving on other entities within the group. All "emoluments" paid to NEDs should be put to shareholders for approval.

■ The writer is an associate professor at the NUS Business School, where he teaches corporate governance and ethics.