COMMENTARY

Progress in corporate governance, but challenges lie ahead

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

AS THE Singapore Governance and Transparency Index (SGTI) enters its 10th year of assessment, it is heartening to note the remarkable progress made by companies over the years. For this year, the average overall score for the general category of companies hits an all-time high of 56.3 from 33.9 in 2009. In the category of real estate investment trusts (Reits) and business trusts, there is a marked rise to 74.5 from 60.4 last year when this category was started.

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

Within the stakeholder engagement section, there were three more glaring omissions. These were: (1) disclosing policies and activities relating to customer health and safety; (2) publishing data on employee training and development; and (3) describing the company's anti-corruption programmes and procedures. In each of these separate aspects, only one-fifth of all companies in the general category fulfil the assessment criteria.

Beyond good overall progress of companies and the specific need for improvement in stakeholder engagement, let us look ahead at the critical concerns in the new corporate governance landscape when the Code of Corporate Governance and Singapore's Exchange Listing Rules are revised. A most fundamental aspect that receives much attention is director tenure and board independence.

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For this year's SGTI, we have an interesting range from new directors who just joined to the very seasoned directors who served more than 50 years (the director with the longest tenure now is on the board for some 55 years). Figure 2 shows the distribution of director tenure.

We made a fascinating observation that director tenure seems to have an impact on independent directors as shown in Figure 3. When director tenure increases, it seems that the proportion of independent directors decreases.

We further examined whether companies making comprehensive assessment of the definition of director independence has any impact on director tenure. In a very revealing way, if companies do not make such independence definition, directors tend to stay longer. On average, when independence definition is made, director tenure is 7.7 years compared to an increased 8.8 years when no such definition is made.

In fact, whether the chairman is independent or non-independent also affects the proportion of independent directors. Companies with independent chairmen have, on average, 54.6 per cent independent directors on the board whereas those with non-independent chairmen have 51.6 per cent.

The observations are very pertinent to gauge our companies' readiness for a scenario when independent directors should form at least one-third of the board as well as the majority of the board if the chair is not independent.

From the current proportion of independent directors in various situations, it appears that the companies are quite ready for the upcoming regulatory requirement. Nevertheless, it is critical to monitor director tenure and chairman independence on a continual basis so as to upkeep the independence of boards.

Board independence has merits that are immense and multi-faceted. It is the highest assurance that the company can be well-managed from the shareholders' and more broadly, the stakeholders' viewpoints.

Interestingly, we tried to ascertain the relationship between the scores in the stakeholder engagement section with director independence. What we found was very illuminating – when the proportion of independent directors goes up, the stakeholder engagement scores increase (see Figure 4).

Even in the three specific areas of improvement needed in stakeholder engagement – customer health and safety, employee training and development, anti-corruption – those companies with higher proportion of independent directors tend to fare better in each of the areas.

So we have a somewhat compelling integrated narrative going forward. In essence, our corporate governance has progressed well over time but we are weak in a particular aspect – stakeholder engagement. In preparing for the new regulatory landscape, we have to address the challenges of director tenure and board independence. In doing so, we can also solve the problem of stakeholder engagement.

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Challenges brew ahead for corporate governance

FIGURE 1. SGTI SECTION PERFORMANCE (GENERAL CATEGORY)

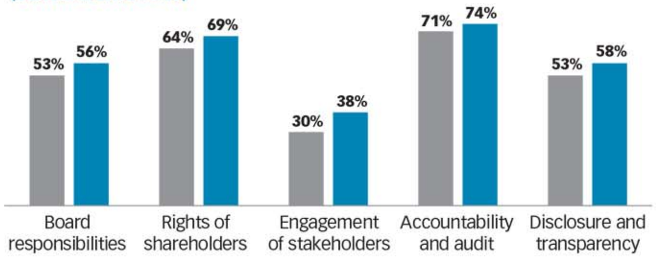


FIGURE 4. RELATIONSHIP OF STAKEHOLDER ENGAGEMENT AND DIRECTOR INDEPENDENCE

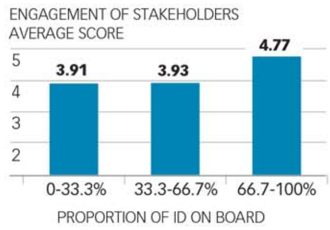


FIGURE 2. DIRECTOR TENURE DISTRIBUTION

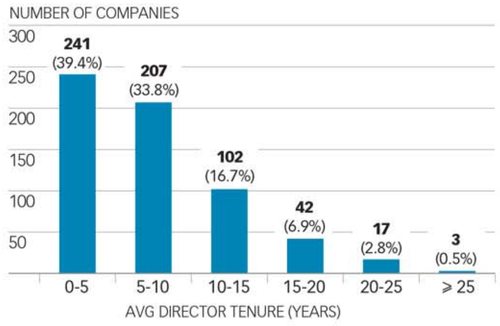
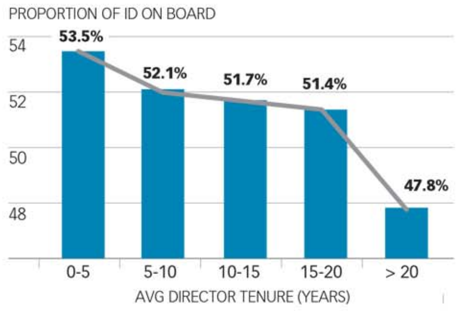


FIGURE 3. RELATIONSHIP OF DIRECTOR TENURE AND DIRECTOR INDEPENDENCE



Source: NUS CGIO

How scoring for the Index is done

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

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

The objective of the SGTI is to evaluate listed companies, including Reits and Business Trusts, on their corporate governance practices and disclosures, as well as the timeliness, accessibility and transparency of their financial results.

For the General Category, the SGTI score has two components: the base score, and the adjustment for bonuses and penalties.

The base score for companies contains five sections: board responsibilities (35 points), rights of shareholders (20 points), engagement of stakeholders (10 points), accountability and audit (10 points), and disclosure and transparency (25 points).

The aggregate of bonuses and penalties is incorporated into the base score to arrive at the company's SGTI total score.

For the Reit and Business Trust Category, the companies are evaluated on a similar set of criteria, but with added coverage on the unique nature of their operations.

The base score for Reits and Business Trusts includes items in the base score for the SGTI (75 points) and trust-specific items in the base score for the SGTI for Reits and Business Trusts (25 points) that focus on structure, leverage, interested person transactions, competency of Reit manager/trustee-manager, and emoluments.

SGTI2018 covers 589 Singapore-listed companies in the General Category as well as 43 Reits and Business Trusts which released their annual reports by May 31, 2018.

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

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