Source: *The Business Times,* p29
Date: 14 January 2020

Without swift enforcement, it would appear that SGX Regco is losing the battle to raise the quality of disclosure and compliance. BT FILE PHOTO: YEN MENG JIIN

Compliance with SGX listing rules is still poor

Incorrect or omitted disclosure of mandatory information has become far too commonplace. BY CHEW YI HONG AND MAK YUEN TEEN

ON OCT 29, 2019, at 7.57 am, Sakae Sushi responded to queries by Singapore Exchange (SGX) issued four days earlier regarding, among other things, the auditors' basis for disclaimer of opinion and the supplemental information on directors who were seeking re-election. The annual general meeting (AGM) was to take place at 3 pm that day, and those who have lodged proxies would have done so before Sakae provided the information.

Sakae was just one of at least 11 issuers in 2019 asked to provide the information required in Appendix 7.4.1 of the SGX Rulebook for each director seeking election/re-election at the AGM, after failing to do so in accordance with the new requirement. This requirement, introduced as part of the SGX rule changes made with the release of the 2018 Code of Corporate Governance, came into effect on Jan 1, 2019.

SGX had opened consultation on the amendments to the listing rules from January to March 2018 and published the final rules on Aug 6, 2018. There was then a transition period of more than four months until the effective date. Yet the 11 issuers above failed to comply.

In fact, unfamiliarity with the new rule was cited by another company when explaining an incorrect disclosure it made. In October 2019, Metech International published its annual report for the year ended June 30, 2019. As its controlling shareholder, chairman and CEO Simon Eng was seeking re-election at its October 2019 AGM, the information required in Appendix 7.4.1 had to be disclosed. Metech stated "negative confirmation" for the question relating to whether Mr Eng has been the subject of any regulatory action, even though he had been publicly reprimanded by SGX at Advanced SCT in October 2015.

On Dec 26, 2019, the second author (Mak) blogged about the incorrect disclosure. Following SGX queries, the company issued a corrigendum to its annual report which showed that not only was he reprimanded at Advanced SCT, he also received a warning from the Monetary Authority of Singapore (MAS) in 2014 on another matter.

Part of Metech's excuse was that the regulatory change was new, even though an annual report published four months earlier by Citicode (formerly Advanced SCT) had disclosed the SGX reprimand when Mr Eng stood for re-election. However, in that case, the warning from MAS was not disclosed. Mr Eng has since resigned from the Citicode board on Dec 31, 2019.

SGX Regco issued a notice of compliance and directed Metech to re-convene an extraordinary general meeting (EGM) to re-elect Mr Eng as it deemed the information to be "inaccurate and incomplete". It also said it will further investigate the matter. While we support SGX Regco's swift action, the company is incurring unnecessary costs which arguably should be borne by the directors, not shareholders. We also wonder about the role of the sponsor in discharging its responsibilities in this episode.

Unfortunately, incorrect or omitted disclosure of mandatory information has become far too commonplace, whether in annual reports or under continuous disclosure obligations. This is despite the teeth that the continuous disclosure regime in Singapore is supposed to possess.

Statutory backing, so what?

Unlike the Code of Corporate Governance which is based on "comply or explain", listing rules are mandatory and must be complied with, unless a waiver is granted by SGX. This was why 12 guidelines in the 2012 Code which are critical requirements or baseline market practices were shifted to the listing rules "for mandatory compliance".

The requirement to comply with the listing rules is contractual in nature, as part of the listing agreement signed between the issuer and SGX. Directors and executive officers also have to provide an undertaking to SGX. Together, the listing agreement and undertaking provide the basis for SGX to enforce listing rules on issuers, directors and executive officers, and to take enforcement actions for non-compliance. Enforcement actions can include public reprimands and fines for issuers, and public reprimands for directors and executive officers. Errant directors can be put on the watch list. SGX can also refer more serious breaches to statutory regulators for further action.

The listing rules are given more teeth through the Securities and Futures Act, which attracts penalties for non-compliance. Section 25 allows MAS, SGX or a person aggrieved by the failure to comply with, observe, enforce or give effect to the listing rules to apply to the High Court to make an order to direct that this be done, after an opportunity to be heard has been given.

Section 203 provides statutory backing to the continuous disclosure requirement in the listing rules while section 199 makes it an offence for any person to make a statement or disseminate information which is "false or misleading in a material particular", subject to the provisions of the section.

Yet, many companies do not seem to be taking the listing and statutory requirements seriously.

The bark

To be fair to SGX Regco, it has been working in overdrive to raise the level of disclosure. Based only on responses to queries that were made public, there were 556 responses to SGX queries posted on SGXNet in 2019. This is an astonishing rate of almost 11 queries on average every week, or more than two queries every trading day.

A total of 256 companies – or just over a third of all issuers – have been queried by the Exchange in 2019. One issuer received 18 separate queries (each query often includes a number of sub-queries). In this case, SGX Regco is spot on in ensuring that sufficient information is available to the market, although this may be too little too late as the company's auditors flagged going concern issues in the middle of last year.

Next is an S-chip with 12 separate queries and another five companies with seven to eight queries. One Fast Track company, who happens to be a Catalist sponsor, received three public queries from the Exchange with regard to the proposed disposal of its operating subsidiary that was the main profit contributor.

While queries do not necessarily mean that a company has failed to comply with its disclosure obligations, they do at least raise the question as to whether the company should have disclosed more in the first place rather than having to be prodded by SGX. Multiple queries, especially relating to the same matter, are likely to be indicative of disclosure deficiencies, potential changes to risk profile or doubts over the commercial substance of transactions.

Doing their own thing

As another indication of the poor compliance with listing rules, consider another change in the listing rules – the requirement to disclose the reasons for non-payment of dividends in the financial statements.

Specifically, Rule 704(24) SGX Listing Rules (Mainboard) and Rule 704(23) of the SGX Listing Rules (Catalist) require that in the event that the board decides not to declare or recommend a dividend, the company must expressly disclose the reason(s) for the decision together with the announcement of the financial statements. This ties in with the updated provision in the 2018 CG Code which states that a company develops its dividend policy and communicates that to shareholders.

To emphasise this new requirement, SGX even underlined the following phrase "together with the reason(s) for such decision" when it announced the changes. It then followed up by updating Appendix 7.2 that issuers use for their reporting with the following phrase "and the reason(s) for the decision" in section 12, which is the relevant section that dealt with the declaration of dividend.

We tracked over 400 companies that reported their half-year results in July to August 2019. This group of companies have a December financial year end, and would have about a year since the finalisation of the amended SGX rules to adjust to the new requirements. For those that did quarterly reporting, this would be the second financial statement published in 2019.

It is shocking that 55 per cent of the companies actually used the old template that did not ask for the reason for the non-declaration of dividends.

While some market participants may argue that it is substance that matters, this displays a lackadaisical attitude to compliance with listing rules, which one would not expect if the issuer is bidding in a tender or submitting an application for licences or government grants.

For those who say that we should look at substance, we disregarded the template used and analysed the responses given by companies. More than 9 per cent of the companies (or 38) simply stated that the section on dividends was "not applicable" when they had not declared dividends, with no explanation. Perhaps shareholders in these issuers should tell the directors that director fees are also not applicable to them!

Nearly a quarter (104 issuers) simply provided statements such as the following: "No dividend has been declared/recommended for the quarter" or "The directors do not recommend any declaration of dividend for the current financial period reported on." This may have sufficed before the rule change when the template simply required the issuer to provide a statement to that effect, but not anymore.

A sixth of the companies stated that they were loss making and just over a sixth said they would conserve cash to fund future investments.

Seven per cent simply stated that it was not the company's practice or policy to declare an interim dividend, while 11 per cent stated that it would only consider at the financial year-end. We think that these two "reasons" given by companies fail the test of substance. As SGX explained in its response to the consultation, the disclosure of the reasons for not paying dividends is a starting point for companies to communicate to their shareholders on their strategy and performance. Shouldn't the directors be giving more substantive reasons than merely stating a practice, policy or intent?

For example, shouldn't they be explaining the growth and cash flow needs and how it may or may not be able to support any dividends to its shareholders, instead of just having the issue come up almost as an afterthought at the end of the financial year?

We noted that queries by SGX Regco were sporadic and non-exhaustive. In our analysis, more than 100 companies either stated that section 12 was "not applicable" or they simply stated no dividend was declared without giving any underlying reason. Yet, we observed that SGX queried just six companies in July and August and only a total of 19 in the whole of 2019.

However, SGX Regco should not have to remind issuers to comply with the rules. What happened to the undertaking signed by directors and key officers which require them to use their best endeavours to procure the issuer to comply with listing rules?

Of the 19 companies queried for not providing the reason for non-declaration of dividends, seven of them have since filed a subsequent quarterly report. Of these seven, only one woke up and switched to the new template. The other six continued using the old template. Four out of the seven now gave the reason for not declaring dividends while three others were still giddily stating that no dividend has been recommended.

Don't bother us

Non-answers to queries are another problem. In December 2019, SGX queried Catalist-listed Alliance Healthcare on its proposed plan to acquire a loss-making startup without commissioning an independent valuation of the target. The proposed acquisition was deemed synergistic but involves a substantial premium to the net asset value. In response to SGX's queries seeking greater clarity on the proposed deal, Alliance simply referred to its original announcement in responding to each of the five queries and did not offer even a tiny nugget of additional information beyond the initial announcement. Alliance was listed only in May 2019 and was already fending off SGX with non-answers. Once again, we wonder about the role of the sponsor in this episode.

In another instance, on Nov 1, 2019, Raffles Education responded to a SGX query which, among others, asked about the independence of a long tenured director and for the "mandatory information in Appendix 7.4.1" for directors going for re-election to be disclosed. Raffles Education replied that the brief biodata of the directors could be found in its annual report, and the full details were disclosed when the directors were first appointed. It also confirmed that there are no changes to the information disclosed in the original appointment announcements and reaffirmed the negative confirmation for all the declaration items.

However, one of the two directors was first appointed in 2008 (the other in 2018) and surely the issuer has the obligation to update his information according to the required Appendix. Specifically, the template asked for the company to provide the director's working experience and occupation(s) during the past 10 years and other principal commitments for the last five years. Yet, Raffles Education pointed to the appointment announcement from 10 years ago.

At the time of writing, the corporate website provided by the company in its annual report appears to be non-functional. Using a search engine, we found another website which appears to be outdated, with announcements from 2012 to June 2018. As SGX has a five-year rolling window for its announcement, how are investors supposed to retrieve the original appointment announcement from 2008? Even if that were possible, we strongly doubt that the 2008 appointment announcement contains all the information asked in the current Appendix 7.4.1.

Will the above responses set a precedent for other issuers? Raffles Education also did not provide a date to SGX's query, which specifically stated "at the upcoming Annual General Meeting". Raffles Education only published its response on Nov 1, 2019, one day after its AGM.

Time to bite

Without swift enforcement, it would appear that SGX Regco is losing the battle to raise the quality of disclosure and compliance. The last public disciplinary action taken by SGX was in November 2018 and the last such action against an issuer and its directors was in July 2018. In 2019, there has not been a single public disciplinary action taken by the SGX disciplinary committee.

Perhaps SGX Regco should be spending less resources prodding companies and directors to do what they are required to do, and more resources taking them to task.

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