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ESG PUSH

Who governs sustainability in companies? The right approach makes the difference

A new report looks at current practices in three regional markets and how companies can adopt the structures that best suit them

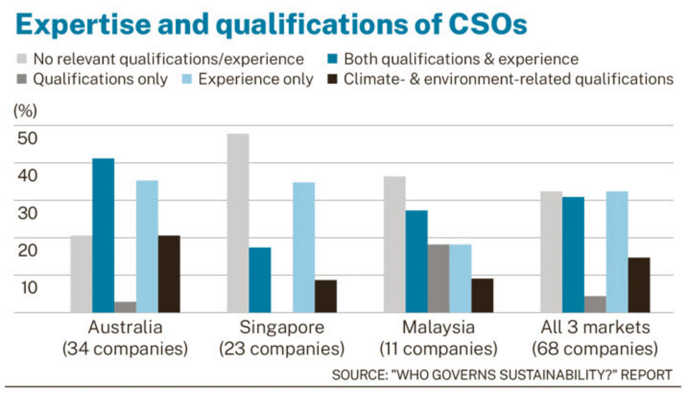
By Michelle Quah
michquah@sph.com.sg

COMPANIES in the region are increasingly building sustainability concerns into their business and governance structures – but they could stand to be more mindful in doing so, such that these arrangements prove both effective and meaningful, according to a new study.

The report, *Who Governs Sustainability?*, looked into two key areas in sustainability governance and practices for 150 of the largest listed companies in Australia, Malaysia and Singapore: 1) the sustainability governance structures adopted; and 2) the appointment, role and attributes of chief sustainability officers (CSOs).

It also challenges companies to consider the issues that would help them to determine the governance structures they should adopt, and whether and how they should appoint a CSO.

"It is time to go beyond sustainability reporting to ensuring that sustainability is built on a solid foundation of good governance," said Professor Mak Yuen Teen of the NUS Business School, who authored the report.



"We see a plethora of structures and practices and, while there is no single approach that works for all companies, certain practices are likely to provide a better foundation for overseeing and managing sustainability risks and opportunities."

The study covered 50 of the largest companies from each of the three countries, and they were from a range of diverse sectors; the smallest company had a market capitalisation of about US$0.8 billion, while the largest was around US$149 billion.

Looking first at disclosure practices, the report said:

■ Most (93 per cent) companies disclosed their sustainability governance structures – 100 per cent in the Malaysian sample, and 90 per cent and 88 per cent for Australia and Singapore, respectively; while

■ Almost two-thirds (66 per cent) also included a chart showing this structure – 86 per cent from Malaysia, 70 per cent from Singapore, and 40 per cent from Australia.

The advantage of including a chart, Mak said, is that it gives a clearer picture of the structure as well as the reporting relationships.

In terms of governance set-ups, the report found that:

■ Thirty-eight companies, in total, have formed a board sustainability committee or equivalent, or expanded an existing committee's description to cover sustainability responsibilities;

■ Most have a non-executive director chairing the board sustainability committee; while 83 per cent of these chairmen in Australia, 55 per cent in Malaysia, and 54 per cent in Singapore are independent; and

■ Two-thirds of the directors on these committees in Australia are independent directors (IDs), while the proportion in the Malaysian and Singaporean companies is under 60 per cent.

The benefit of having independent elements on these committees is that it could mitigate potential conflicts of interest; executive directors on board sustainability committees might have to implement sustainability policies they advised on, or manage other concerns such as remuneration policies that may be affected by sustainability policies.

As for whether companies should have a separate board sustainability committee, Mak said there is no single "best practice" sustainability governance structure applicable to all.

> **"...Apart from having a moral obligation to act responsibly, how corporates respond to sustainability considerations will determine their survival in the long term."**
>
> Eugene Wong, chief executive officer at Sustainable Finance Institute Asia

"An additional committee does not mean a company will be more effective in addressing sustainability risks and opportunities, (and) there is a risk of fragmentation of the board's responsibilities if there are too many different committees."

But he added that there are two sustainability governance structures that can be considered for most companies.

One is to integrate sustainability responsibilities into multiple existing committees – this might apply to companies for whom sustainability factors are not so material as to cause significant reputational or financial harm. The board would need to ensure these committees' responsibilities are well-articulated, and that they have a sufficient focus on sustainability issues.

Another option – to form a separate board sustainability committee – would be for companies where certain environmental, social and governance (ESG) factors are critical to their business or provide potential opportunities for growth. This committee should work with other existing ones that are expected to embed ESG considerations into their responsibilities.

"Investors should also pay closer attention to the expertise and experience of board committees, and whether they tap on independent advice if they do not have sufficient expertise/experience – not just whether they have a separate committee," Mak added.

The report also looked into the appointment of CSOs, and found that:

■ Australian companies were more likely to appoint a CSO, with 68 per cent having done so, compared to 46 per cent in Singapore and 22 per cent in Malaysia;

■ Across the three countries, 62 per cent of the CSOs are women;

■ More than half (58 per cent) of the companies that appointed a CSO did not indicate who they report to, which leaves their seniority and the substantiveness of their roles unclear; but 69 per cent are said to have a dedicated role;

■ The proportion of CSOs that are internally versus externally appointed is comparable across the three countries, with internal appointments ranging between 61 and 65 per cent; and

■ About 62 per cent of the CSOs have held ESG-related roles prior to their current role; others most commonly had prior experience in strategy and innovation, operations and investor relations/communications.

As for what companies should look for in a CSO when appointing one, Mak acknowledged the ongoing debate on the merits of having someone with company-specific or ESG expertise.

"I believe that if climate risk is a critical ESG risk for a company, like an oil & gas company, then the CSO or certainly someone very senior in the function needs to have a good understanding of the science. For large companies with a sustainability department or function, having a good diversity of expertise and experience relevant to the most material ESG factors is useful.

While there is no ideal governance structure that applies to all companies, certain practices provide a better foundation for managing sustainability risks and opportunities, says Prof Mak Yuen Teen. PHOTO: BT FILE

"I lean towards ESG expertise and experience first, particularly those areas most important to the company. It's like appointing a COO (chief operating officer), CFO (chief financial officer) or another C-suite position. They can get to learn the business after they are hired."

Calling the report "a tour of options for corporates to select a governance approach that best suits their needs", Eugene Wong, chief executive officer at Sustainable Finance Institute Asia (SFIA), which partnered Mak in the study, said companies have to move beyond treating sustainability as a peripheral consideration.

"Indeed, it must be integrated into the soul of every corporate and their governance structures. Having the right philosophy and living up to it through an effective structure involving the right people and processes are imperative. Apart from having a moral obligation to act responsibly, how corporates respond to sustainability considerations will determine their survival in the long term."

This report is the first in a series looking at several aspects of ESG-related practices of regional companies; the next will focus on sustainability assurance, while the one after that will look at materiality assessment of ESG factors.

The full report will be available on Mak's website (*https://governanceforstakeholders.com*) and on SFIA's website (*https://www.sfinstitute.asia/*).