Corporate boards blamed for US turmoil

Risks not managed, say experts, but they warn against over-regulation

CORPORATE governance experts meeting here yesterday have blamed boards of directors as culprits in the global financial crisis.

They claim that directors could – and should – have played a bigger role in managing and mitigating the risks that financial institutions took on in the high-risk trading of complex credit derivatives.

But they are now worried that a knee-jerk reaction will lead to over-regulation.

The remarks came on the sidelines of yesterday’s inaugural Investors’ Corporate Governance Conference organised by the Securities Investors Association of Singapore (SIAS) held at the Raffles City Convention Centre.

Professor Steen Thomsen, director of the Centre for Corporate Governance at the Copenhagen Business School, said that boards which were supposed to supervise management did not have sufficient financial expertise.

This was especially apparent with regard to understanding the risks involved in complex financial instruments such as credit derivatives – what Mr Warren Buffett termed “financial weapons of mass destruction”. And ignorance meant a lack of regulation.

Professor Mak Yuen Teen, co-director of the Corporate Governance and Financial Regulation Centre at the National University of Singapore’s Business School, said the risk managers at the financial institutions were essentially overpowered by risk takers.

Risk managers, such as a board of directors or internal auditors, could be seen as holding back firms from making money by their prudence, he said.

Prof Mak said a board of directors must provide checks and balances and make management understand the risks involved in any strategy while providing a plan to mitigate these risks.

However, this is difficult especially when a company is doing well. He said that “it would be difficult for the board to pour cold water on the good news and say let’s take stock of where we are”. Both experts agreed that over-regulation must be avoided.

Prof Thomsen said that the financial industry has been heavily regulated already so more rules will not solve the problem.

Rather it is an issue of having the right regulation, which means having capital reserve requirements tailored to the risks that the banks take on, he said.

“We need to have regulators appreciate those risks and set standards for those. I’m afraid there will be over-regulation if we focus on everything between heaven and earth,” he added.

Prof Mak said the “pay for performance” system that rewards management with large cash bonuses needs to be balanced with risk management.

“It is good to have incentives, but it is also important to factor in risk into a CEO’s performance bonus,” he added.