A toothless code is better than no bark

The voluntary Corporate Governance Code can still help raise awareness

BY YASMINA YAHYA

COMPANIES here will undergo changes in the coming months, with sweeping amendments expected to the Companies Act.

The proposed changes have received positive responses from the corporate world — from company directors, lawyers and accountants.

While this is a wide-ranging review, covering areas from director duties and shareholder rights to redefining serious fraud, changes to the voluntary Corporate Governance Code (CGC) have attracted their fair share of debate too.

This code comprises a list of recommendations to Singapore-listed companies on issues from transparency, accountability, disclosure of top executives’ pay and board composition, to how a company should communicate with its shareholders.

Unlike the Companies Act, which is law, the CGC is not mandatory. Companies can either comply with the code or explain in their annual reports why they have decided not to.

This is the point of most contention. Several experts on corporate governance have called for the CGC to be given more teeth. They think that this may be one way to more effectively stem the constant tide of corporate scandals that have been making headlines here.

To recap a few of the most recent:

In mid-July, the provisional liquidator of Celestial Nutrifoods disclosed troubling governance lapses by the firm. The specialist team of accountants and lawyers that studied Celestial’s assets and liabilities to help it prepare for a winding-up found a transfer of funds from the supposedly insolvent firm to a third party.

Shareholders were powerless to express their dismay — the China-based maker of soy and biofuel products has been suspended from trading since 2009 and has since been told to delist, while facing a winding-up petition.

Meanwhile, special auditors appointed to investigate accounting irregularities at fabric producer China Gaoxian have since found that the company is missing 1 billion yuan ($187.2 million) from its bank accounts.

And electronics manufacturer KXD Digital has filed a police report against its former chief executive and chairman, Mr Liu Fusheng, for possible fraud and breach of the listing rules, as well as failures of corporate governance.

A recent study conducted by the Centre for Governance, Institutions and Organisations (CGIO) of the National University of Singapore (NUS) Business School found that most Singapore-listed firms fulfil only the minimum requirements of the CGC.

The CGIO came up with a checklist of things that a company should do in order to meet basic corporate governance standards. A company that meets all the minimum requirements would earn 100 points. It then allocated bonus points whenever a company went beyond these basic standards.

If a company had corporate governance concerns in the past year, however, it would be penalised.

The scores generated by the study showed that only two Singapore-listed companies — SingTel and Singapore Exchange (SGX) — met all the basic requirements and went beyond them.

SingTel received the highest score of 109 while the SGX earned 101 points. Alarmingly, only 46 out of the 597 companies earned at least 50 points.

According to Associate Professor Lawrence Loh from the department of strategy and policy at the NUS Business School, some received negative scores.

Some may be tempted to conclude from this that a toothless corporate governance code does not do much to boost transparency, accountability and standards among Singapore firms. But it is useful to look at it from another standpoint.

Having the code, toothless or not, gives investors a benchmark to measure locally listed firms against and determine where to invest.

And as NRA Capital managing director Kevin Sculley notes, that the CGC is not mandatory makes it all the more meaningful when a company does comply.

Even if a company cannot be taken to court for not complying with the code, it can be punished in the stock market.

Several studies show a correlation between the strength of a company’s corporate governance standards and its share valuation.

The Singapore Management University (SMU) conducted such a study last year, which found that SGX-listed companies with the lowest corporate governance standards tended to trade below asset value.

Companies with the highest governance standards, meanwhile, traded on average 1.4 times asset value.

Thanks in part to the publication of such research, retail investors are becoming more aware and demanding.

Investor relations executives at many Singapore-listed firms have noticed that retail investors are asking more — and tougher — questions at shareholder meetings in the last few years.

And despite the fact that the CGC is not mandatory, companies are also aware that it makes business sense for them to comply.

“Good companies with a high standard of corporate governance will gladly disclose that they observe the code in order to differentiate themselves from the bad companies,” says SIM University’s Associate Professor Chan Yoke Kai.

“The market will also be able to differentiate the good from the bad. Bad companies with a low standard of corporate governance in turn will attempt to level up,” SingTel’s chief financial officer, Ms Jeanne Low, says, complying with the code “allows us to attract capital at the lowest cost, attract professional and independent directors, and recruit and retain our talents.”

It might be a long time, if ever, for the CGC to become mandatory by law.

But, if it does, it will contribute to raising as much awareness in the next decade as it has in the last, that might be good enough.

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