Truth, justice, and the corporate way

A good board should have attributes such as integrity, mix of competencies, commitment, and diversity of viewpoints

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Headline: Truth, justice, and the corporate way
Source: The Business Times, p21
Date: 19 July 2012

ALL of us must have watched The Avengers and Captain America. What some investors expect of independent directors (IDs) is like Captain America: strong, courageous, and noble, who only think of the wellbeing of others and not about themselves. They could do almost the impossible. So, the expectations of some investors about IDs are very high.

In contrast, some IDs think of themselves as Superman because they sit on so many boards and it seems that they can rush at the speed of a bullet from one meeting to another even when those meetings are held at the same time. When things become difficult, these Superman-IDs quite often resign, citing other commitments or to pursue their personal interests. It’s like Superman confronted by kryptonite.

Investors sometimes get IDs who carry the title of an ID but who are actually there to help the management of the controlling shareholder. In some cases, IDs appear totally aligned with the controlling share- holders and management. They behave contrary to what their public face and “independence” label suggest. They are like Two-Face – with a good public face and a darker private side.

Some IDs are very competent and committed but they see a controlling shareholder. A good ID needs a good board to be truly effective. You can’t make a good ID even if the whole board is made-up of Jokers, even Batman would have a problem.

What makes a good board? Clearly, the board needs to have sufficient power to oversee management and safeguard the interests of the company, and with clearly defined roles and responsibilities.

Resides, there are important board processes and practices such as the selection of directors, board renewal, induction, and professional development, which affect the effectiveness and functioning of a board. A good board should have high standards. Even so, there should be attributes such as the board’s commitment to the company and its diversity of viewpoints.

Diversity is very important for an effective board. Can you imagine the Avengers with six Hawkeyes? If you look at the Avengers, such a team brings a different set of skills to the team. There is also gender diversity in the Avengers. My point is that diversity is important to a board just as it is to the Avengers and the Justice League.

To close the expectations gap for IDs, there can be suggestions to the interests of the company. There is a need to clarify the flying rules or code of corporate governance that IDs have a secondary duty, so as to safeguard the interests of minority shareholders.

Finally, all controlling shareholders or management who are represented on the board would certainly be lacking after their own interest. IDs need to be there to provide a check and balance on behalf of minority shareholders.

Appointee and removal of IDs: We should consider changing the composition of the nominating committee to include non-board members and minority shareholders’ nominees, like the Swiss model. The current composition of the nominating committee puts the selection of directors, including IDs, in the hands of incumbent directors and controlling shareholders.

Most countries have provisions to allow minority shareholders holding a certain percentage of shares to nominate directors to the board, but when it comes to election of directors, the controlling shareholder almost always gets to decide who actually gets onto the board.

Some countries have increased the ability of minority shareholders to elect at least one ID. Another possibility is to subject the election and removal of IDs to higher thresholds of support by shareholders, so that there is sufficient support from minority shareholders.

Hong Kong and Malaysia have now recommended that IDs who are to be retained beyond nine years should be subject to a separate vote by shareholders. However, such a vote will be largely superfluous if controlling shareholders get to vote and if only majority (more than 50%) support is required.

Remuneration of IDs: IDs need to be remunerated fairly and appropriately. If you expect people to commit their time and utilize their expertise to help the company, they won’t do it for free. After all, they are not Captain America.

I have often heard that the remuneration of IDs is too low in Singapore. This is a generalization. Some large companies are paying their IDs more than $200,000 per year, although they are more commonly in the $100,000 to $150,000 range (after taking into account basic retainers, additional fees for being chairs or members of committees, and meeting fees).

Considering the relative size and complexity of Singapore companies and the risk that directors are exposed to compared to the more developed markets, this level of fees does not appear to be uncompetitive.

Further, it is still quite common for companies here to allow IDs to participate in share-based remuneration schemes, such as share option plans, and often, there is little transparency about the total remuneration paid to IDs because the value of these share- based awards are not properly reflected in the remuneration paid to these directors and formally approved by shareholders.

Paying fairly and transparently must go hand-in-hand.

Election of director duties: In addition to remuneration, which is the “weight” in the form of the director’s duties, IDs who breach their duties must be taken to task. Some markets have developed a range of sanctions, including criminal, civil, and administrative sanctions (such as reprimu- nds, disqualification, and blacklisting of directors). I am delighted to see that Singapore is now doing more to enforce directors’ duties.

Some complain that the recent enhanced enforcement actions against directors in Singapore have made it very risky to be directors of listed companies. The reality is that enforcement actions are still for “outli- er” cases involving egregious behavior or gross negligence.

We are still a long way from the kind of rigorous regulatory or share- holder enforcement actions that we see in developed markets like Austral- ia and the US.

Stricter rules on becoming and remaining an ID: There ought to be more stringent criteria for becoming a director, especially an ID, with a steering committee reviewing our company list that we should not impose minimum academic or professional qualifications to become a director.

However, the current low thresholds for becoming and remaining as a director, especially an ID of a listed company, need to be reconsidered.

In addition to sufficiently strict criteria and processes for determining independence and commitment of di- rectors, it should be mandatory for di- rectors to undertake training and profes- sional development, before they be- come directors – and on an ongoing basis.

If we find it difficult to gain acceptance for imposing mandatory training on incumbent directors, then we can “grandfather” directors with a certain number of years of experience on listed companies. We need to act quickly to improve the professional- ization of directors, especially IDs.

When I was an accountant stu- dent more than 30 years ago, there was already a debate on the expecta- tion gap for auditors. Today, that gap remains as wide as ever. Given the lack of any comprehensive and re- buttal action by regulator’s world- wide addressing the effectiveness of IDs, I expect that 30 years from now, we will still be having a big expecta- tion gap for IDs.

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