

The Directors'

# Bulletin

SID  
SINGAPORE INSTITUTE OF DIRECTORS

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## Board Evaluation

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*Member of The Bank of East Asia Group*

4 Shenton Way #14-02  
SGX Centre 2  
Singapore 068807  
Tel : 65 6227 2838  
Fax : 65 6227 9186  
Email: secretariat@sid.org.sg

Website  
www.sid.org.sg

Publisher  
Singapore Institute of Directors

Editor  
Michael Grenville Gray

Design  
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Publication & Website  
Sub-committee

Chairman  
Yeoh Oon Jin  
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Qualvin Advisory Pte Ltd

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## From the Editor

This edition of the SID Bulletin revolves around the role of the nominating and remuneration committees with a focus on the recruitment of and the evaluation of the performance of directors. Annabelle Yip considers the procedures for selecting and rewarding directors with particular emphasis on matching skills and competencies of existing and potential directors to that needed by the organization and the measures to be used by the remuneration committee in fixing remuneration packages.

Whilst nominating committees can be found in most listed companies in Singapore, how many have implemented a proper formalised system for evaluating the performance of the Board? It is fair to say, probably not very many. The article by Geoffrey Keel and James Beck sets out clearly seven key questions that boards should consider when planning an evaluation, the importance of such an evaluation and the benefits. This is followed by SID statement of good practice on board evaluation.

Two articles on the issue of accounting scandals follow. The first considers two recent court cases in Singapore, which have an impact on the liabilities of auditors and directors in situations where fraud has been perpetrated on a company. The other shows the link between corporate failures and the lack of adequate internal controls.

In general, there has been a dearth of women on boards of Singapore listed companies. The feature 'The Women's Register: Matching the talents of women leaders to the needs of the community' introduces the Women's Register, which is a useful resource for locating women who are qualified to sit on boards.

Finally David Sandison raises an issue which is very pertinent to those who are non executive directors (NEDs), particularly those so called 'professional directors', whose income is mainly from directors fees. This is the fact that NEDs, unlike the self employed and those under contracts of employment, are not able to obtain tax relief on CPF contributions made. He has put forward some suggestions that could rectify this anomaly. ■

*Mike Gray*

**Mike Gray**  
Editor

## SID Governing Council 2007/08

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## President's Message

Dear Members,

As this issue of our Bulletin is the first for this year I would like to inform you of some of your Institute's recent and forthcoming activities.

For those of us who were able to attend the recent Singapore Corporate Awards Gala Dinner last month, I am confident that you will agree with me that it was indeed a most fitting finale to many months of planning and hard work by the many members of the Organising Committee and the various judging panels. Your Institute was once again very much part of this annual event which is organized to encourage, promote and recognize excellence in board practices, corporate leadership and organisational performance, financial management, investor relations and corporate disclosure and transparency. Your Institute would like to salute all the winners, both corporate and individual, for being outstanding role models in this community and thank the Singapore Exchange and the Business Times for organising and supporting this great event.

Your Institute was once again the lead organiser for the Best Managed Board Award and for the Chief Executive Officer of the Year Award. I would like to thank our partners, AON Consulting and Egon Zehnder International for their superb support and contributions in co-organising these two awards with us. Our special thanks also go to Mr. Lim Chee Onn and Professor Tommy Koh who were both kind enough to chair the respective judging panel.

Within the next few weeks, the Institute will launch its regular Singapore Board of Directors Survey. It will be our 6th survey, with the last one conducted in 2006, on board practices of SGX-listed companies. The latest survey will not only provide information on board practices but also trends and changes over the years since the survey was first conducted in 2000 and how corporate governance practices have evolved since then. For this latest survey, we will again be partnering SGX, Egon Zehnder and PricewaterhouseCoopers.

Over the next 4 to 5 months we will be embarking on what is likely to be one of the most important initiatives in the 10 year history of your Institute. With the support of the Monetary Authority of Singapore, SGX and ACRA we will be undertaking a strategic review of



our current and future role and direction. While much has been achieved by your Institute in recent years your Council believes more needs to be done in order that your Institute will remain relevant, effective and focused in the future and continue to play a significant role in helping Singapore retain her position as a leading global financial and commercial centre. Your Council has therefore decided, with the support of MAS, SGX and ACRA, to appoint PricewaterhouseCoopers to undertake this strategic review. As there was a delay in the appointment of the consultant the final report is now expected in July/August of this year.

On behalf of SID I would like to acknowledge and thank MAS, SGX and ACRA for their support and commitment in making this initiative possible.

As mentioned in my message in the last issue of our Bulletin, this is the 10th year of your Institute's formation and a series of events is being planned to celebrate this 10th anniversary which will culminate with a gala dinner towards the end of the year. Details of these events will be announced early in the second quarter and we hope many of you will play an active role in these events.

This issue of our Bulletin features board evaluation as its main theme. This subject has been given increased attention and importance as more and more companies realise the importance of evaluation to improved performance. Your Institute has long held the position that the effective selection and appointment of well qualified directors and the continued and systematic evaluation of their performance, both individually and collectively as a group will contribute much to the effectiveness of the Board and the success of the company. We hope you will enjoy reading these articles and find them beneficial.

May I on behalf of your Council wish each one of you and your organisations continued success in 2008. ■

Thank you and warm regards.

**John KM Lim**  
*President*

# Selecting Your Directors, Paying Them Fairly: Looking at the Work of Nominating and Remuneration Committees



By Annabelle Yip  
Partner  
WongPartnership LLP

In a booming economy and tight labour market, the attracting and remuneration of talent has been a key issue for many companies. The same forces have been at work for companies seeking to grow their boards. However, in addition to the economic factors at play, tightened corporate governance initiatives have a significant influence on the search and remuneration of directors.

On the one hand, the increased responsibilities and liabilities have resulted in many directors limiting the number of board seats that they take on. On the other hand, companies are having to search in a smaller pool of talent in view of the greater performance expectations that heightened corporate governance has placed on boards.

The procedures for selecting and rewarding directors have also had to undergo a sea change, with an increased focus on transparency and accountability. In other countries, where shareholder activism has been burgeoning and hefty salaries have created a sense of scandal, companies are increasingly being asked to justify their choices and their pay structures. In these countries, private equity funds and other institutional investors too have stepped in to demand greater disclosure from their boards, and have not hesitated to recommend voting against a resolution if they do not agree with it.

While these trends have yet to arrive at Singapore's shores in a big way, it is nevertheless still useful for directors and companies to take a hard look at how directors are chosen and rewarded. The Singapore Code of Corporate Governance ('Code') sets out principles and guidelines for this, and this article will not rehearse the guidelines in the Code. Instead, it will examine the very practical steps needed to transform these guidelines into usable and working policies.

## Appointment and Nomination of New Directors

Principle 4 of the Code states that there should be a formal and transparent process for the appointment of new directors to the Board. It also recommends the establishment of a nominating committee, and this is now considered standard practice for most listed companies. However, the Code goes no further in setting out just how the nominating committee is to operate. This is of course reflective of the fact that there is no one-size-fits-all approach, and each company must determine the process that suits its size and needs as well as the functions and responsibilities to be vested in the nominating committee.

Notwithstanding this, many listed companies have established best practices in the nomination and appointment process. For companies looking to formalise and adopt similar arrangements, there can be no better place to start than to examine and adapt these existing methods. This structuring and formalising process is also important as the Code recommends that a description of the process for the selection and appointment of new directors to the Board should be disclosed (Guideline 4.5 of the Code).

### *Self-Examination: A Necessary First Step*

Any nomination and appointment process should start with a review of the company's business, and its business plans and goals for the medium-term. This is not simply a question of a software company, say, looking for someone with a technology background. A company who is looking to expand into regions with strong labour protection laws may want someone familiar with dealing with trade unions, or someone with a legal background, or someone who has had experience in the particular jurisdictions. In

times of expansion, a company may want someone with experience in mergers and acquisitions; in times of downsizing, a company may want someone who has experience with retrenchment.

Having determined the terrain, the nominating committee should then examine the existing board members. This review process may mean not only looking at their experience, and their skills and competencies, but could also include a review of their personalities, networks and contacts. Examples of skills sets and characteristics that a nominating committee may wish to consider include the following:

- a willingness to challenge management;
- special expertise;
- expertise on global issues;
- an understanding of key technologies;
- external contacts valuable to the company;
- a detailed knowledge of the industry;
- high visibility in the field; and
- a strong ability to represent the company to stakeholders.

The review should be widened to cover not only the board members as individuals, but also their composition as a group. Is the board too heavily weighted in favour of any one discipline? Are all the board members dynamic go-getters who might need a more restraining influence?

### *Skills and Competencies Needed*

The nominating committee will then need to sit down to correlate the information in order to determine the qualities of the person or persons needed to provide a suitably balanced board. A set of skills and strengths should be compiled, distinguishing between qualities that are needed and those that are merely desirable.

Increasingly, a required component of this skills set will be the ability to read and understand a financial statement. This need arises partly from the need to give a negative assurance statement on the company's interim financial statements under rule 705(4) of the Listing Manual. However, more importantly, it is the result of the Court of Appeal's decision in *PlanAssure PAC v Gaelic Inns Pte Ltd* that it is incumbent on even non-executive directors "to at least perform a minimal degree of oversight in relation to the accounts and seek to be regularly apprised of the [company's] financial affairs". In this respect, it would seem that while the court will not require all directors to have a detailed understanding of accounting and finance, they should have a basic financial literacy to be able to broadly discern if any irregularities exist on the face of the accounts.

### *Short-listing Suitable Candidates*

With this list, the nominating committee can begin to compile a long list of candidates that on their face meet some or most of the requirements listed. At this stage, the nominating committee should consider whether it would be useful to work with an executive search firm. If this is not the preferred route, the committee should in any event seek to canvas candidates from as many sources as is both possible and practicable. Existing board directors are one good source, but other sources should be explored as well. This helps to broaden the search and ensure that the list is not confined to the persons that board members already know and are friendly with. While collegiality on the board is an important factor in its ability to accomplish results, some diversity and independence will also be needed to avoid the risk of the board becoming an echo chamber.

The long list may now be reviewed in order to narrow the search to a

short list of five to ten candidates. As a simple first step, the nominating committee should simply determine if there are any candidates that should be taken off because of any conflict or independence issues. In this respect, regard must be had to Guideline 2.1 of the Code which sets out the circumstances which will preclude a director from being considered independent. The nominating committee should also bear in mind that it has the discretion to determine that a director is non-independent even if he does not fall under any of these circumstances (Guideline 4.3 of the Code). The converse, of course, is also the case.

It is also useful at this juncture for the committee to also check whether any of the candidates is already sitting on too many boards to be able to devote sufficient time to the work of this board. This is in line with Guideline 4.4 of the Code which stipulates that when a director has multiple board representations, he must ensure that sufficient time and attention is given to the affairs of each company. What is too many will depend on the amount of work that is expected from the directors. Larger, more complex companies will likely need their board members to be able to spend more time reviewing documents.

Whether any of the candidates should be removed from the long list due to relationships with existing directors is also something that may usefully be considered at this stage. After all, every new board member that is appointed is also a reason for existing board members to stay or go.

#### *Selection: The Final Step*

With this pared down short list, the nominating committee will then need to carry out a detailed due diligence on the remaining candidates. Their

track records, references, and profiles should be carefully assessed. It is useful for the nominating committee to seek the input of the chief executive officer at this stage as to his preferences in this regard (although some committees may prefer to seek his involvement at an earlier stage to avoid any last minute setbacks)

It is only finally at the end of this long process can the nominating committee begin meeting and interviewing candidates. If possible, meetings with the chief executive officer and other directors should be factored in as well. Some companies may wish to have the candidate spend some time at corporate headquarters to get a feel for the organisation. After all, both sides will, at the end of the day, be making an assessment of character, commitment, and fit.

### Remunerating Directors

Principle 7 of the Code states that there should be a formal and transparent procedure for developing policy on executive remuneration and for fixing the remuneration packages of individual directors.

The Code does set out some general guidelines on how a remuneration policy should be designed. For example, Guideline 7.1 recommends the setting up of a Remuneration Committee. Guideline 8.1 recommends that the performance-related elements of remuneration should be designed to align the interests of executive directors with those of shareholders and link rewards to corporate and individual performance. However, these general precepts must still be translated into a formalised and structured remuneration policy if they are to be implemented.

As with the appointment of directors, many multinationals and large listed corporations already have established

formalised written policies. It is useful therefore to take a look at current methods and practices for determining remuneration.

#### *The Measure of the Man*

In most cases, a key issue to be addressed in any remuneration policy will be the measurement of performance. The traditional measures have been numeric: growth in shareholders' net worth, earnings per share, or increases in market share. Increasingly, however, companies are concerned that such measures focus too closely on short-term gain, and lose sight of long-term strategic performance and sustainability. From a corporate governance and legal perspective, a more holistic approach, incorporating both qualitative and quantitative criteria, and measuring individual performance as well as the collective





performance of the board as a whole, has much to commend it as being more in line with the duty of directors to act in the company's best interests. A strategy that produces a short-term gain but sacrifices the company's medium- or long-term future could well be contrary to such interests.

Traditional measures are being supplemented with other extra-financial measures. The specific type of extra-financial measure or measures used will depend on the company, its business, its goals, and the composition of the board. For example, some companies use an appropriate measure of customer satisfaction as an extra-financial measure. A company in the construction industry may, for example, use corporate safety performance as an extra-financial measure. Some measures may

be applicable more to executive directors than non-executive directors who play no part in management. Measures may need to be developed and tailored according to the particular role of the director in the company. The intent is to determine what areas of performance are critical to the company's success and to encourage or incentivise their development.

#### *Applying the Measures*

Once these measures have been determined, then the remuneration committee needs to consider how much weight should be accorded to them so that they provide a meaningful incentive towards fulfilment. In this respect, linking performance in these areas to benefits such as share options or deferred bonus schemes may be considered as a means of tying in performance with actual real world results. This approach is endorsed by Guideline 8.4 of the Code which encourages the use of long-term incentive schemes.

For extra-financial measures, depending on what is being assessed, companies may prefer to rely on independent third parties to provide this assessment. Customer satisfaction may, for example, be determined by customer satisfaction surveys. Where an aspect of the measurement of performance which impacts on remuneration is peer opinion, independent consultants also provide an important element of discretion and confidentiality.

#### *Putting a Number on It*

Regardless of the policies designed, the remuneration will eventually have to be pegged to a number. In determining the appropriate figure, Commentary 8.5 of the Code has this to say: "In setting remuneration packages, the company should be aware of pay and employment

conditions within the industry and in comparable companies. But they should use such comparison with caution, in view of the risk of an upward ratchet of remuneration levels with no corresponding improvements in performance."

A useful place for the remuneration committee to start will be to determine what comparably sized companies in the same industry are paying. In this respect, the requirement to disclose bands of directors' pay will help the committee to decide on a figure. Executive consultancy firms can also provide useful data, and their assistance may be particularly needed where the comparables are overseas corporations. The remuneration committee will need to decide whether such external expertise needs to be brought in for them to make their determination.

#### **Conclusion**

Companies may balk at the initial effort of putting together such policies for remuneration. However, given the central and guiding leadership role played by the directors of the board, this effort will surely pay off as a well-led, transparent company will be attractive to shareholders and investors. ■



# Seven Steps to Effective Board and Director Evaluations



By Geoffrey Kiel  
Professor, Queensland University of Technology  
Founder and Chairman  
Competitive Dynamics Pty Ltd



By James Beck  
Managing Director  
Competitive Dynamics Pty Ltd

Board assessment is too often viewed as a necessary evil – a mechanical process of checking off items on a list that ultimately has little real value for the board apart from meeting compliance requirements. However ... an effective board assessment process has the potential to be transformational.<sup>1</sup>

When a corporate scandal occurs, such as those experienced at China Aviation Oil (Singapore) Corporation Ltd in 2005, it is to the board that the shareholders, media, regulators and community look for answers. As the ultimate decision-makers in the corporation, the board is responsible for the corporation's actions and performance.

The challenge for boards today is to add value to the organisations they govern. Performance evaluation is a means by which boards can ensure they have the knowledge, skills and ability to meet this challenge. This is recognised in numerous best practice guides and standards. For example, the Singapore Code of Corporate Governance first introduced by the Corporate Governance Committee in 2001 and revised in 2005, states that: "There should be a formal assessment of the effectiveness of the Board as a whole and the contribution by each director to the effectiveness of the Board".<sup>2</sup>

This article will provide a practical approach to effective board and director evaluations using a seven-step framework that asks the key questions all boards should consider when planning an evaluation.

Even good boards can benefit from a well-conducted evaluation. As summarised in Table 1, a properly conducted evaluation can contribute significantly to performance improvements on three levels: the organisational, board and individual director levels. It must be stressed, however, that these benefits can only be achieved through a properly executed board evaluation; if incorrectly executed, an evaluation can lead to distrust among board members and between the board and management.

Table 1 Potential benefits of board evaluation<sup>3</sup>

Benefits	To organisation	To board	To individual directors
Leadership	<ul style="list-style-type: none"> <li>• Sets the performance tone and culture of the organisation</li> <li>• Role model for CEO and senior management team</li> </ul>	<ul style="list-style-type: none"> <li>• An effective chairperson utilising a board evaluation demonstrates leadership to the rest of the board</li> <li>• Demonstrates long-term focus of the board</li> <li>• Leadership behaviours agreed and encouraged</li> </ul>	<ul style="list-style-type: none"> <li>• Demonstrates commitment to improvement at individual level</li> </ul>
Role clarity	<ul style="list-style-type: none"> <li>• Enables clear distinction between the roles of the CEO, management and the board</li> <li>• Enables appropriate delegation principles</li> </ul>	<ul style="list-style-type: none"> <li>• Clarifies director and committee roles</li> <li>• Sets a board norm for roles</li> </ul>	<ul style="list-style-type: none"> <li>• Clarifies duties of individual directors</li> <li>• Clarifies expectations</li> </ul>
Teamwork	<ul style="list-style-type: none"> <li>• Builds board/CEO/management relationships</li> </ul>	<ul style="list-style-type: none"> <li>• Builds trust between board members</li> <li>• Encourages active participation</li> <li>• Develops commitment and sense of ownership</li> </ul>	<ul style="list-style-type: none"> <li>• Encourages individual director involvement</li> <li>• Develops commitment and sense of ownership</li> <li>• Clarifies expectations</li> </ul>
Accountability	<ul style="list-style-type: none"> <li>• Improved stakeholder relationships (e.g. investors, financial markets)</li> <li>• Improved corporate governance standards</li> <li>• Clarifies delegations</li> </ul>	<ul style="list-style-type: none"> <li>• Focuses board attention on duties to stakeholders</li> <li>• Ensures board is appropriately monitoring organisation</li> </ul>	<ul style="list-style-type: none"> <li>• Ensures directors understand their legal duties and responsibilities</li> <li>• Sets performance expectations for individual board members</li> </ul>
Decision-making	<ul style="list-style-type: none"> <li>• Clarifying strategic focus and corporate goals</li> <li>• Improves organisational decision-making</li> </ul>	<ul style="list-style-type: none"> <li>• Clarifying strategic focus</li> <li>• Aids in the identification of skills gaps on the board</li> <li>• Improves the board's decision-making ability</li> </ul>	<ul style="list-style-type: none"> <li>• Identifies areas where director skills need development</li> <li>• Identifies areas where the director's skills can be better utilised</li> </ul>
Communication	<ul style="list-style-type: none"> <li>• Improves stakeholder relationships</li> <li>• Improves board-management relationships</li> <li>• Improved board-CEO relationships</li> </ul>	<ul style="list-style-type: none"> <li>• Improves board-management relationships</li> <li>• Builds trust between board members</li> </ul>	<ul style="list-style-type: none"> <li>• Builds personal relationships between individual directors</li> </ul>
Board operations	<ul style="list-style-type: none"> <li>• Ensures an appropriate top-level policy framework exists to guide the organisation</li> </ul>	<ul style="list-style-type: none"> <li>• More efficient meetings</li> <li>• Better time management</li> </ul>	<ul style="list-style-type: none"> <li>• Saves directors' time</li> <li>• Increases effectiveness of individual contributors</li> </ul>

Although boards may differ in the severity of their governance problems and the range of issues they face, there are still a number of key decisions that are relevant to all boards implementing an evaluation process. An effective framework relies on the board reaching agreement on the answers to the seven key questions illustrated in Figure 1. While these questions must be asked for all board evaluations, the combined answers can be quite different. Therefore, while the questions are common to each, evaluations can range markedly in their scope, complexity and cost.

Although the framework below is depicted sequentially, in practice most boards will not follow such a linear process. Some of these decision areas will be reached simultaneously; for example, 'Who will be evaluated' may be decided at the same time as 'Who will conduct the evaluation'. However, at some point, each of these questions will need to be answered.

Figure 1 Framework for a board evaluation<sup>4</sup>



## Step 1: What are our objectives?

Step 1 is to establish what the board hopes to achieve. Clearly identified objectives enable the board to set specific goals for the evaluation and make decisions about the scope of the review. Such issues as the complexity of the performance problem, the size of the board, the stage of

organisational life cycle and significant developments in the firm's competitive environment will determine the issues the board wishes to evaluate. Similarly, the scope of the review (how many people will be involved, how much time and money to allocate) will be determined by the severity of the problems facing the board and the availability of sufficient resources to carry out an evaluation.

The first decision for most boards to consider is the overriding motivation for the evaluation process. Generally, the answer to this question will fall into one of the following two categories:

- corporate leadership – for example, 'We want to clearly demonstrate our commitment to performance management', or
- problem resolution – for example, 'We do not seem to have the appropriate skills, competencies or motivation on the board'.

## Step 2: Who will be evaluated?

Comprehensive governance evaluations can entail reviewing the performance of a wide range of individuals and groups. Boards need to consider three groups:

- the board as whole (including committees)
- individual directors (including the roles of chairperson), and
- key governance personnel.

Considerations such as cost or time constraints, however, often preclude such a wide-ranging review.

Alternatively, a board may have a very specific objective for the review process that does not require the review of all individuals and groups identified. In both cases, an effective evaluation requires the board to select the most appropriate individuals or groups to review, based on its objectives. To make this decision,

we recommend that a list of possible review participants be gradually filtered down to a pragmatic selection of review subjects.

A common issue in deciding who to evaluate is whether to concentrate on board-as-a-whole only or also include individual director assessment. Regular board-as-a-whole evaluation can be seen as a process that ensures directors develop a shared understanding of their governance role and responsibilities. Although board-as-a-whole evaluation is excellent as a familiarisation tool for inexperienced boards, one disadvantage is that group evaluation may give only limited insight into any performance/governance problems. Consequently, some boards choose to progress to the evaluation of board committees, individual directors and the chairperson to gain greater insight into how their board is functioning.

To gain an objective view of individual director performance, peer evaluation is preferable, since by having members of the board evaluate each other, it is possible to gain a more holistic picture of the strengths and weaknesses of each director and their contribution to the effectiveness of the board. It can also be used to identify skills gaps on the board or communication issues between directors. Should an individual director evaluation be conducted, it is paramount that the outcomes of this review be correlated with the whole-of-board outcomes to validate the appropriateness of any recommendations.

## Step 3: What will be evaluated?

Having established the objectives of the evaluation and the people/groups that will be evaluated to achieve those objectives, it is then necessary to elaborate these objectives into a number of specific themes to ensure

that the evaluation:

- clarifies any potential problems
- identifies the root cause(s) of these problems, and
- tests the practicality of specific governance solutions, wherever possible.

This is necessary whether the board is seeking general or specific performance improvements, and will suit boards seeking to improve areas as diverse as board processes, director skills, competencies and motivation, or even boardroom relationships. We suggest boards consider their specific objectives in light of a leading practice governance framework to establish the roles the board is expected to fulfil (see Table 2, for an example).

Table 2 Generic roles of a board<sup>5</sup>

Board role
1. Strategy
2. CEO
3. Monitoring
4. Overview of risk management
5. Overview of compliance
6. Policy framework
7. Networking
8. Stakeholder communication
9. Decision making
10. Effective governance

Of course, a comprehensive list of areas for investigation will need to be balanced with the scope of the evaluation and the resources available for the project. At this stage a realistic assessment of the resources available, a component of which is the time availability of directors and other key governance personnel, can be made.

#### Step 4: Who will be asked?

The vast majority of board and director evaluations concentrate exclusively on the board (and perhaps the CEO) as the sole sources of in-

formation for the evaluation process. However, this discounts other potentially rich sources of feedback. Participants in the evaluation can be drawn from within or from outside the company. Internally, board members, the CEO, senior managers and, in some cases, other management personnel and employees may have the necessary information to provide feedback on elements of a company's governance system. Externally, owners/members and even financial markets can provide valuable data for the review. Similarly, in some situations, government departments, major customers and suppliers may have close links with the board and be in a position to provide useful information on its performance.

After examining all potential sources of information along with their relative advantages and disadvantages, the facilitator must decide which sources to include in the review. This requires an understanding of three issues:

- in light of the specific questions identified in the previous step, who has the knowledge needed to make a valid and reliable assessment
- what is the level of board experience with, and openness to, the evaluation process and what is the impact on who should be asked, and
- what resources are available to collect the information from the required sources.

#### Step 5: What techniques will be used?

Depending on the degree of formality, the objectives of the evaluation, and the resources available, boards may choose between a range of qualitative and quantitative techniques. Quantitative data are in the form of numbers. They can be used to answer questions of how much or how many. Questions of 'what', 'how', 'why', 'when' and 'where' employ

qualitative research methods.

Most boards undertake evaluations without a clear view of the issues before them. When the evaluation's objectives are to identify the key governance problems, screen alternative solutions and/or uncover new approaches, qualitative research comes to the fore. Qualitative data does, however, have several drawbacks.

The major drawback is that interpreting the results requires judgment on the part of the person undertaking the review and analysis. This is best addressed by using experienced researchers for the task and having several participants review the conclusions for bias. Bias can also be mitigated by using both quantitative and qualitative techniques.

The three main methods used for collecting qualitative data in governance evaluations are interviews, board observation and document analysis:

- the interview provides a unique opportunity to collect complex and rich data. It is an excellent way of assessing directors' perceptions, meaning and constructions of reality by asking for information in a way that allows them to express themselves in their own terms
- observation of a board meeting is especially useful when the evaluation objectives relate to issues of boardroom dynamics or relationships between individuals
- documents can also be a rich source of information in the governance evaluation process. It can be a method of triangulation for use in conjunction with other data collection techniques.

While quantitative data lack the richness of qualitative data, they have the advantage of being specific and measurable. Surveys are by far the most common form of quantitative technique used in governance

evaluations and can be an important information-gathering tool. It is vital to understand, however, that surveys are attitudinal instruments.

There is no best methodology. Research techniques need to be adapted to the evaluation objectives and board context.

## Step 6: Who will do the evaluation?

The next consideration is to decide who the most appropriate person is to conduct the evaluation. If the review is an internal one, the chairperson may conduct the evaluation.

However, for reasons of impartiality there are times when it may be more appropriate to delegate either to a non-executive or lead director, or to a board committee. Depending on the previous steps, and decisions made in Step 7 as to the audience for the results, mature boards are more frequently considering engaging in external evaluations to provide a level of independence and advice to proactively improve overall governance and board dynamics.

In the case of external evaluations, specialist consultants or other general advisers with expertise in the areas of corporate governance and performance evaluation lead the process. However, the specialised nature of a board review often requires skills outside the customary scope of many general advisers. Similarly, a consultant engaged specifically to carry out the evaluation can be perceived as more independent than a reviewer with an existing relationship with the firm (such as a general counsel or auditor). Specialist consultants will also have a broad range of exposure to different boardroom practices and performance benchmarks.

One compromise between the two

approaches is to utilise an online board evaluation to confidentially develop an evaluation report that can be delivered by the chair or lead director.<sup>6</sup>

## Step 7: What do you do with the results?

The review's objectives should be the determining factor when deciding to whom the results will be released.

Most often the board's central objective will be to agree a series of actions that it can take to improve governance. Since the effectiveness of an organisation's governance system relies on people within the firm, communicating the results to internal stakeholders is critical for boards seeking performance improvement. Given that virtually all governance reviews are conducted with a view to improving the governance system, boards are rarely faced with the decision of whether to communicate the results internally. Rather, the decision is who within the organisation needs to know the results.

Since the board as a whole is responsible for its performance, the results of the review will be released to the board in all but the most unusual of circumstances. Where the evaluation objectives are focused entirely on the board, board members will simply discuss the results among themselves. Normally, the board, CEO and company secretary will review the findings around the boardroom table, and there may be no need to communicate the results to anyone else. Where the results of the evaluation concern individual director performance, the generally accepted approach is for the chairperson and/or facilitator to discuss them individually with each director. Directors may be asked to discuss their own results around the board table, a process that can lead to a

much greater extent of mutual understanding.

In circumstances where the objective of the board evaluation is to assess the quality of board-management relationships, results of the evaluation will generally be shared with the senior management team. Some organisations choose to communicate a summary of the board evaluation results more widely in the organisation.

In certain circumstances, the board will have an objective of building its reputation for transparency and/or developing relationships with external stakeholders. In such circumstances, the board should consider communicating some or all of the results of its review to those stakeholders. Communicating the results of the evaluation demonstrates that the board takes governance seriously and is committed to improving its performance. Obviously a balance needs to be struck between transparency on the one hand and the need for owners or members to retain faith in the board's ability and effectiveness on the other hand.

## In summary

Aside from the seven key questions in an evaluation, boards need to consider how often they should evaluate their performance. The annual review is the most commonly recommended form of assessment. However, a predictable annual event can become stale and no longer add value; therefore, it is important to experiment with different evaluation styles and techniques to keep the process interesting and ensure that it continues to lead to performance improvements.

Performance evaluation can be an ongoing process, not just an annual event. High-performing boards tend to devise other mechanisms apart

from an annual review to ensure ongoing performance improvement. One option is to review the effectiveness of each board meeting. This is a simple technique for keeping performance issues 'front of mind' for the board. It is an easy way to gain quick feedback and to encourage discussion and interaction between board members, and it requires little time or effort to put in place.

Performance evaluation is becoming increasingly important for boards and directors and has benefits for individual directors, boards and the companies for which they work. Boards also need to recognise that the evaluation process is an effective team-building, ethics-shaping activity. Our observation is that boards often neglect the process of engagement when undertaking evaluations; unfortunately, boards that fail to engage their members are missing a major opportunity for developing a shared set of board norms and inculcating a positive board and organisation culture. In short, the process is as important as the content.

*This article is published with the permission of Dr Geoffrey Kiel and James Beck. They can be contacted on +61 7 3510 8111 or via email on [advisors@effectivegovernance.com.au](mailto:advisors@effectivegovernance.com.au) or [James.Beck@effectivegovernance.com.au](mailto:James.Beck@effectivegovernance.com.au) respectively.*



## Notes

<sup>1</sup>Nadler, D A, Behan, B A, and Nadler, M B, Building Better Boards: A Blueprint for Effective Governance, Jossey-Bass, San Francisco, 2006, p230

<sup>2</sup>Corporate Governance Committee, Code of Corporate Governance 2005 - Board Matters, Principle 5, <http://www.asc.gov.sg/attachments/CodeofCorporateGovernance.doc>

<sup>3</sup>Kiel, G C, Nicholson, G J, and Barclay, M A, Board, Director and CEO Evaluation, McGraw-Hill, Sydney, 2005, pp 13-14

<sup>4</sup>Kiel, Nicholson, and Barclay, 2005, p 17

<sup>5</sup>For an elaboration of these roles see [www.effectivegovernance.com.au/](http://www.effectivegovernance.com.au/) and select 'Services/Board Evaluation'

<sup>6</sup>For more information on online evaluations see [www.effectivegovernance.com.au/](http://www.effectivegovernance.com.au/) and select 'Online Products'

# Singapore Institute of Directors Statement of Good Practice Board Evaluations

## 1 Introduction

1.1 Principle 5 of the Code of Corporate Governance 2005 ('Code') recommends that there should be a formal assessment of the effectiveness of the Board of Directors ('Board') as a whole and the contribution by each director to the effectiveness of the Board. Guideline 5.2 of the Code further recommends that the Nominating Committee should decide how the Board's performance may be evaluated and propose objective performance criteria which should be approved by the Board.

1.2 Conducting board evaluations are increasingly becoming a norm internationally. With the passing of the Sarbanes-Oxley Act of 2002 in the United States, the New York Stock Exchange ('NYSE') adopted standards requiring boards of companies listed on the NYSE to conduct and disclose the results of board evaluations]. The NYSE also requires that the various board committees, and in particular the audit, nominating and remuneration committees, include in their terms of reference specific provisions on conducting evaluation of their respective performances.

1.3 Board evaluations are not mandatory in Singapore. However, the provisions as contained in the Code recommending the assessment and evaluation of the Board and its members have been around since the time the Code came into force.

1.4 There are clearly tremendous benefits to conducting regular board evaluations. However, the members

of the Board should be aware of the risks that may arise if the board evaluation process is not carefully designed.

1.5 This Statement of Good Practice provides guidance on why board evaluations should be undertaken, the benefits and risks of board evaluations, and how the evaluation should be undertaken. Note that this Statement of Good Practice assumes that the board itself will be involved in the setting up of the actual evaluation process. No "bottoms-up" approach (ie, of staff or management evaluating the board) is proposed at this time.

## 2 What Are Effective Board Evaluations?

2.1 Board evaluations are processes of, whether formal or informal, identifying the effectiveness of a board in relation to how board members work with each other, how the board works with management, how the board as a whole has coordinated its efforts and marshalled the company's resources to increase or improve upon the performance of the company.

2.2 To be clear, a board should not be assessed only upon whether the company has become more profitable; the board can also be assessed on how it has dealt with a crisis for example.

## 3. Why Undertake Board Evaluations?

3.1 One purpose of board evaluations



is to allow the board as a whole and the directors individually to identify any possible gaps that may exist in the work undertaken by the Board and to identify ways of improving the process.

- 3.2 Another important reason for undertaking board evaluations is to assess how the board and the individual directors work together with each other and with other stakeholders of the company. To this extent, board evaluations aid in fostering communication amongst the directors and between the board and management on various matters, including corporate strategy, board composition and board processes.
- 3.3 A further important purpose of evaluations is to identify the "best" fit in board composition with the ultimate aim of increasing shareholder value.

#### 4 Benefits And Risks Of Board Evaluations

##### 4.1 Benefits

- 4.1.1 Improves director effectiveness by identifying gaps, if any, and correcting them.
- 4.1.2 Improves Board collegiality through the exchange of views on how the board as a whole is performing.
- 4.1.3 Helps the Board to focus on how it operates and identifies areas that can be improved.
- 4.1.4 Helps the Board to focus on long-term strategies.
- 4.1.5 Provides a written record to show that the Board is diligent in monitoring its own actions.

##### 4.2 Risks

- 4.2.1 Written records of the Board evaluation process may be discoverable in litigation, with the possibility that

negative conclusions not acted upon possibly being used adversely during the litigation.

- 4.2.2 Responses to written questionnaires for evaluation may not reflect the overall perspective of the Board.

#### 5 Designing The Board Evaluation

- 5.1 There is no standardised design for board evaluations and each board should be careful about adopting an evaluation process prepared by another company for its own use.

- 5.2 Board evaluation materials must be designed as appropriate to each board. Boards should be mindful of the issues that, in the opinion of the Directors, such an evaluation process should address, the information that they want to gather, as well as the retention policy of the feedback that is received from the board members.

- 5.3 One of the most important aspects of the evaluation process is to elicit a frank evaluation of the board's operations and performance from the directors, both individually and as a group.

- 5.4 In designing the board evaluation process, the use of subjective questions should be avoided wherever possible.

- 5.5 Broadly, any board evaluation design should at least take into consideration the following:
- (a) Board culture
  - (b) Board composition
  - (c) Board procedures and processes
  - (d) Information flow and accessibility
  - (e) Leadership on the board and how this is transmitted
  - (f) Management interface
  - (g) Shareholder interface and communications

- 5.6 Additionally, the board evaluation

design should also take into account the following two major areas, although external market conditions could also play a part:

- (a) Company-related factors, including the size of the company, the nature of its business, the complexity of the operations, profitability, the structure and responsibilities assigned to the board, and the risks and challenges of the business.
- (b) Director-related factors, including qualifications and experience of the directors, their availability (in terms of being able to attend meetings or at least provide feedback as may be required), involvement and actual participation at meetings, and additional responsibilities assigned to the relevant directors, including whether he is a chair or member of a sub-committee of the Board.

5.7 The Nominating Committee, whether on its own or with the assistance of external consultants, should be tasked with the design and formatting of the evaluation process. The Nominating Committee in designing or working with external parties to design the evaluation process, must ask: 'What is the purpose of the evaluation?' or 'What is it that we want to achieve?'

5.8 The Nominating Committee must further identify, in the course of preparing the evaluation process, what factors constitute success to the company. In doing so, they should also identify the external factors that could have an impact on these success factors, the relevant information that is necessary to carry out the evaluation and the appropriate tools needed to carry out the evaluation.

5.9 In this regard, the Code suggest that

relevant performance criteria that may be used could include the company's share price performance over a five-year period vis-à-vis the Singapore Straits Times Index and a benchmark index of its industry peers return on assets, return on equity, return on investment and economic value added over a longer-term period. As far as the relevant criteria in assessing the individual directors are concerned, the key factors include whether the individual director continues to contribute effectively and demonstrate commitment to the role (including commitment of time for board and committee meetings, and any other duties).

5.10 The Nominating Committee, working in conjunction with the Board, should also be tasked with determining who should be given the responsibility of conducting the evaluation, ie whether it should be done internally by another committee, by the Nominating Committee, by self-evaluation, or by an external consultant, as well as whether the process is intended to be conducted through a written questionnaire or via oral interview.

5.11 The Nominating Committee should determine how the company's record retention policies and practices should be applied to the data gathered in the course of the evaluation process and it should ensure that such record retention procedures are strictly adhered to.

## **6 Conducting And Gathering Information From The Board Evaluation**

6.1 There is no definitive method for conducting a board evaluation. This can be done through a written questionnaire or through oral discussions, with someone recording the responses provided. The written

questionnaire may be the preferred approach as it will ensure consistency from year to year, and will generally be easier for board members to respond to, if properly structured.

6.2 The board and director evaluation should be conducted at least once a year.

6.3 On the basis that a written questionnaire is to be provided, each director should be asked to respond to the same standardised questionnaire relating to the performance of the Board. The preferred and perhaps easiest approach is to have each director also be provided with a questionnaire pertaining to his performance to respond to. Some companies may prefer peer critiques as a form of assessment as well. Whilst this is to be welcomed, it is not something that companies would typically prefer given the deference that each director has to the other and the wish not to offend.

6.4 The information gathered from the questionnaires must be objectively analysed and feedback collated. There are queries as to whether this should be conducted anonymously or by say the remuneration committee. There is no one answer fits all, and the better approach is to always have this conducted internally in the first instance if the review is to be transparent in any event.

6.5 Based on the feedback gathered, changes should be recommended to improve the workings of the board. It must be recognised that not all suggested changes need be or can be implemented immediately. There may be good reasons to introduce changes in a gradual manner and in the order of priority of need.

6.6 The board as a whole should be involved in the decision-making

process as regards the relevant next steps.

6.7 The Board, in conjunction with the NC Chairman, should take appropriate steps to counsel, or at worse, replace non-performing or errant directors.

6.8 The Code recommends that the process used to assess the effectiveness of the board as a whole and the contribution of each individual director to the effectiveness of the board, should be disclosed in the company's annual report. It is not necessary in all cases to disclose the detailed findings of the performance evaluation to shareholders or in the annual report. The degree of disclosure should be left to each company to decide on.

## 7 Conclusion

7.1 This Statement of Good Practice has provided only broad recommendations as regards how a board evaluation can be undertaken. It is imperative to note that there is no one approach fits all and hence no sample appraisal form has been provided.

*This Statement of Good Practice is issued by the Singapore Institute of Directors (the "SID") purely as a guide for its members and with a view to raising standards of corporate governance. The SID takes no responsibility for the accuracy or completeness of this Statement and the reader should obtain independent professional advice regarding any specific set of facts or issues. No part of this Statement may be reproduced (with or without any alteration or modifications) without the prior written consent of the SID. ■*

# Court of Appeal Considers Directors' Duties of Supervision and Management



By Joy Tan, Partner,  
Wong Partnership LLP

The Singapore Court of Appeal recently issued two important decisions both dealing with the scope of duties and liabilities of auditors and directors where fraud has been perpetrated on a company. These two decisions, issued on the same day and covering similar issues, will clearly become important touchstones in future. In brief, the Court of Appeal decided in both cases that:

- in carrying out a statutory audit, auditors have a duty to be alert to fraud and must assiduously investigate any suspicious matters; and
- the quantum of liability imposed on auditors should be reduced by

50% as the company's directors and management should have been able to catch the fraud but failed to do so due to negligence.

The two cases, *JSI Shipping (S) Pte Ltd v Teofoongwongclong* (a firm) and *PlanAssure PAC v Gaelic Inns Pte Ltd*, are examined in this article, which considers in particular their significance and implications for directors.

## Facts of *JSI Shipping (S) Pte Ltd v Teofoongwongclong* (a firm)

The defendant was an accounting

firm that provided audit services to the plaintiff during the financial years ("FY") 1999, 2000 and 2001. The plaintiff was the Singapore subsidiary of an American freight-forwarding company. It had two directors. One was based in Singapore, while the other resided in the United States and was also the head of the plaintiff's ultimate holding company.

The Singapore-based director had overall control and responsibility of the plaintiff's day-to-day operations in Singapore and reported to the US-based director on operational and business issues. It subsequently transpired that the Singapore-based director was engaged in a scheme to

siphon off the plaintiff's profits for his own benefit. His activities were not discovered by the defendant, and they only came to light after one of the staff "blew the whistle" on him to the US-based director.

The plaintiff eventually sued the defendant for negligence in carrying out its audit duties. It alleged that the defendant had failed to pick up the fraud of the Singapore-based director in three principal areas:

- failure to verify the Singapore-based director's entitlement to remuneration;
- failure to report abuses by the Singapore-based director of his cheque signing limit; and
- failure to properly verify the renovation expenses of the plaintiff's warehouse in Singapore and of its Hong Kong subsidiary.

### Facts of PlanAssure PAC v Gaelic Inns Pte Ltd

The plaintiff was a company that ran a pub. Its finance manager had misappropriated company funds through teeming and lading. This process essentially involved delaying the banking of cash received on the day of sales in order to hide misappropriations. Hence, instead of banking the cash received from a particular day's takings into the company's bank account, the finance manager would use the cash for her own personal benefit. The cash used would be replaced subsequently with cash received from subsequent sales. The teeming and lading was carried out substantially over 2003 and 2004.

Sometime in February/March 2004, as part of its audit of the plaintiff for FY2003, the defendant audit firm obtained a copy of the plaintiff's

bank reconciliation statement as at 31 December 2003. This was provided for the purpose of carrying out the audit of bank balances. From the statement, the auditor noticed that the amount of cash deposits which had not been banked into the plaintiff's bank account ("unlodged cash deposits") stood at more than S\$600,000. He then asked the group finance manager for the dates on which the cash deposits were cleared and lodged into the bank account. However, unsurprisingly, this information was not forthcoming. By May 2004, the amount misappropriated had increased to some S\$1 million.

When the misappropriation was eventually discovered, the finance manager was charged and convicted. The plaintiff then commenced a suit against the auditor for negligence, asserting that he had been negligent in failing to spot the misappropriations and to warn management that the high levels of unlodged cash deposits indicated a risk of fraud. It asserted that if the warning had been made, management would have been alerted in good time to prevent further losses and to recover the misappropriated sums from the finance manager.

### Overview of Decisions in Both Cases

On the specific facts of these two cases, the Court of Appeal held that the auditors had not done enough to verify the propriety of the companies' finances given the red flags that were raised during the audit process. Specifically, in JSI Shipping (S) Pte Ltd v Teofoongwonglcloong (a firm), the Court found that the defendant had failed to obtain independent verification of the Singapore-based director's entitlement to

remuneration. In PlanAssure PAC v Gaelic Inns Pte Ltd, the Court found that the defendant had failed to rigorously investigate the possibility of fraud given the unusually large amount of the unlodged cash deposits.

For directors, however, the cases raise important issues as to their duties of management and supervision. This is because, in both cases, the quantum of liability was reduced, and by the significant proportion of 50% in both cases. In broad terms, the Court decided to reduce the auditors' liabilities because it was of the view that the directors and management of the companies had themselves been negligent. However, the legal routes used to achieve this result differed:

- In JSI Shipping (S) Pte Ltd v Teofoongwonglcloong (a firm), the quantum of liability was reduced pursuant to section 391 of the Companies Act. This section allows a court to grant relief to auditors under the circumstances specified.
- In PlanAssure PAC v Gaelic Inns Pte Ltd, the Court found that the directors, executive and non-executive alike, had not looked at the company's accounts. If they had reviewed the accounts, even cursorily, the large amounts of unlodged cash deposits would have been immediately obvious and would have alerted them that something was amiss. This amounted to contributory negligence by the plaintiff.

### Decision in JSI Shipping (S) Pte Ltd v Teofoongwonglcloong

In JSI Shipping (S) Pte Ltd v Teofoongwonglcloong (a firm), the Court noted that the US-based

director never even looked at the plaintiff's audit reports. They referenced one incident whereby the Singapore-based director had sent the original sets of audit reports to the US-based director to be signed by him. In doing so, he stated that he had already signed the reports. The Court noted that this had been done in order to lull the US-based director into a false sense of security by implicitly representing that everything was fine. Separately, the Court also noted that the US-based director had been happy to rely on the perceived good work of the Singapore-based director in building up the business of the company, trusting him wholly and implicitly.

The Court then relied on section 391 of the Companies Act to grant relief to the defendant. As noted above, this section empowers the court to relieve a person either wholly or partly from his liability for negligence if certain conditions are satisfied. These conditions are:

- he has acted honestly and reasonably; and
- having regard to all the circumstances of the case, he ought fairly to be excused for the negligence.

It was accepted that the defendant had acted honestly. As to whether his actions had been reasonable, the Court held that reasonableness for the purposes of section 391 encompassed wider considerations, and could include the conduct of the company's directors. Here, the Court characterised the US-director's conduct as a "general indifference, laxity in management and failure to properly carry out his fundamental obligation to oversee and monitor the [plaintiff-company]".

It should also be highlighted that this alleged indifference and laxity was also relied on by the Court to decide that the auditor's negligence had not caused certain losses. In making a claim for damages, the plaintiff had claimed that but for the defendant's negligence, it would have discovered the frauds relating to the split cheques and warehouse renovations. However, the Court noted that the US-based director had been content to leave everything to the Singapore-based director, and that even after he had been notified of the possible fraud, he took such a long time to react that the Singapore-based director had been able to abscond. Accordingly, the Court held that these omissions broke the chain of causation linking the defendant's negligence to the plaintiff's losses in these two respects.

## Decision in PlanAssure PAC v Gaelic Inns Pte Ltd

In PlanAssure PAC v Gaelic Inns Pte Ltd, the Court relied on the concept of contributory negligence to reduce the quantum of damages for which the defendant was liable. It is important to note that the High Court had excused the non-executive directors of contributory negligence, but found the managing director negligent in failing to even look at the monthly bank reconciliation statements which he received. The Court of Appeal indicted all three of negligent behaviour.

In doing so, it did not rely on whether the directors received or even reviewed the bank reconciliation statements. It noted that as directors, it was incumbent on them to at least perform a minimal degree of oversight in relation to the plaintiff's accounts and seek to be regularly apprised of its financial

affairs. While they were not obliged to delve into minute irregularities in the accounts, they were obliged to broadly discern if any irregularities existed on their face. The Court also noted that even a cursory monitoring of the bank statements would have immediately revealed that something was seriously amiss in relation to the banking in of collections from customers.

The Court also found the company to have been contributorily negligent from the acts and omissions of the accounts and payroll manager. It noted that she had prepared the monthly bank reconciliation statements and had regarded the increasing amounts of unlodged cash deposits as suspicious but failed to do anything about it.

## Additional Observations on Directors' Duties

The following observations of the Court on the responsibility of directors and management should be highlighted:

- It clarified that non-executive directors are not exempted from the need to exercise a certain level of scrutiny of the companies on whose boards they sit.
- While directors cannot be made to bear personal responsibility in all cases for the accuracy and integrity of all of a company's financial statements, both executive and non-executive directors cannot nonetheless shy away from the fundamentals of putting in place prudent arrangements to oversee the preparation of such statements. In this respect, it should be noted that the Court held, in PlanAssure PAC v Gaelic Inns Pte Ltd, that the non-executive directors

were not entitled to wholly rely on the finance manager to ensure that the accounts were in order, and that, in this regard, it was irrelevant that they lacked accounting expertise.

- The duties of auditors and directors to check on management are not wholly distinct and separate, the one beginning where the other ends. Instead, these duties are overlapping, and auditors and directors share a dual responsibility to ensure their discharge. Importantly, the Court noted that effective corporate governance requires both sets of professionals to assiduously discharge their responsibilities

### Significance and Implications for Directors

Companies, directors, and management will wish to take



particular note of the Court's reduction in the quantum of the defendants' liabilities. It is worthwhile noting that in both cases, liability was reduced by 50%. This was perhaps intended to send a signal that responsibility between auditors and directors for financial statements is shared equally between both parties.

More importantly, by characterising the responsibilities of auditors and directors as overlapping, the decisions suggest that directors, executive and non-executive alike, cannot simply rely on auditors but must exercise a certain degree of supervision and oversight in reviewing the company's accounts. Again, it is worthwhile pointing out that the Court seemed to view the frauds as being readily apparent, and would have leapt out at anyone making even a cursory examination of the accounts.

The implications for a failure by directors in this regard can be severe, not only for the company but for the directors themselves. In *JSI Shipping (S) Pte Ltd v Teofoongwonglcloong* (a firm), the Court noted that the defendant had not sought to rely on contributory negligence and characterised its defence in this regard as "sorely lacking". It should be noted that, as a company can only act through its human agents, if contributory negligence is found, it can only have arisen from negligence by its agents. This can only be the directors, managers, or employees. This in turn gives rise to a risk that the director, manager, or employee may in turn be found liable to the company for this negligence.

In a case decided earlier in 2007, *Nagase Singapore Pte Ltd v Ching Kai Huat & Ors*, the High Court held that

while a court would be reluctant to fault a director who had in good faith delegated his functions or powers to competent subordinates, this did not mean that the director could never himself be held negligent because the loss complained of resulted from the negligence of his subordinates whom he bona fide believed to be competent. Even if they had proved themselves to be competent, a director or senior manager must have in place a proper system of ensuring that his subordinates do not make serious mistakes and that such mistakes, if committed, are quickly spotted and rectified.

It is likely that the issue and extent of proper delegation and supervision will become an increasingly important issue for directors in the near future. These recent decisions suggest a trend by the courts to impose strict duties of supervision on management and directors (executive and non-executive). As a practical measure to avoid liability, and as a best practice, boards and companies should consider setting up rigorous systems of checks and review, and to adhere scrupulously to such systems on a continuing basis. Any such adherence should be documented in order to maintain a record of steps followed. ■

# How Soundly Do You Sleep At Night?

Corporate accounting scandals that have rocked boardrooms and global capital markets around the world since the start of the millennium seem to have never left us. The million dollar question then would be why such corporate failures occur both internationally and in Singapore.



By Yong Jiunn Siong  
Advisory Partner  
PricewaterhouseCoopers



A multitude of possibilities including both internal and external factors could be drivers for such corporate failures. However, in most cases, the following scenarios (often in combination rather than singularly) may have provided the breeding ground for corporate failures:

- Weak or non-existent internal controls over area(s) of business operations
- Unnecessary pressure on individuals to perform and/or financial incentives that encourage inappropriate behaviours
- Absence of adequate monitoring controls further compounded by individuals in charge who may not have sufficient knowledge in these high-risk areas
- Management disregard for existing internal controls

Often, these corporate failures occur spectacularly only because of late detection which failed to mitigate significant losses to companies.

### Corporate governance reform in the United States

Arising from the wake of corporate failures at Enron and Worldcom, the Public Company Accounting Reform and Investor Protection Act, also known as the Sarbanes-Oxley (SOX) Act was passed in July 2002 in the United States (US). SOX was designed to improve the quality of financial reporting and corporate governance and restore the loss of investor confidence in the US financial markets. Chief Executive Officers (CEOs) and Chief Financial Officers (CFOs), commonly referred to as the "C-Suite", together with Boards of Directors, and Audit Committees (AC)

in particular recognised their roles and responsibilities to investors. If internal control problems were not rectified in a timely manner, US public companies could face Securities Exchange Commission (SEC) enforcement actions.

Transparent and reliable financial statements are sometimes taken for granted and its importance to investors has never been more apparent nor relevant than today. Current situations in other parts of the world are stark examples of this and these markets are learning the painful lesson that investors will react to unexpected news.

### Legislative response in the US

In the US, SOX required companies to evaluate the effectiveness of their internal control over financial reporting (ICOFR) and added the annual requirement that the C-Suite and their external auditors certify that the companies' internal controls were effective. SOX also required the C-Suite to certify quarterly that the financial information in their reports were fairly presented and did not contain any untrue statements or omissions. Senior management and top managers were made accountable for problems the companies encountered and the C-Suite were responsible for establishing, maintaining and designing internal controls with respect to the preparation of financial statements with the AC having oversight over them.

Good ICOFR increases the reliability of financial reporting and gives CEOs and CFOs the confidence in signing off the results of the company. This in turn gives greater confidence to

investors who rely on the results when making their investment decisions.

What evolved out of the SOX implementation process surprised many ACs. The detailed implementation process, comprising scrutiny of internal controls, financial reporting and accounting methods unearthed problems in the way companies operated and other deficiencies at even the best of companies. Some of these problems are notably:

- Little or insufficient internal controls surrounding the management and timely reporting of business and operational risks which could potentially result in significant financial losses.
- Personnel related problems, in particular the lack of qualified finance and accounting staff, insufficient segregation of duties and inadequate training/supervision.
- Ineffectiveness of accounting information systems leading to revenue recognition and other accounting/reporting issues.
- Lack of standardisation of processes/controls which increases the risk of misstatements in the financial statements. For many global companies which had expanded operations into countries with differing cultures, business practices and in particular standards on financial reporting, this created a time bomb waiting to explode. SOX forced the standardisation of accounting processes and policies resulting in fewer financial errors.
- Too many controls were being performed manually despite the

fact that many companies were using sophisticated financial reporting systems. Generally, when controls are automated and the human element is removed, the risk of (human) error and fraud is reduced

- Excessive access to applications, systems and sensitive data. Even when access control policies were in place, they were found to have been enforced haphazardly. Some SOX compliant companies have automated the management of user identities throughout their organisation (helping enforce compliance and limiting access of sensitive data to authorised users only) and including access controls into coordinated business processes.

All of the above problems prevent the proper functioning of a company's internal control system. It is worth noting that these problems were disclosed by the largest companies in the world.

## A cost higher than compliance

While the SOX implementation costs may be high, the cost of corporate failure is higher. The collapse of Enron, Worldcom and other companies resulted in an estimated US\$8 trillion decline in market capitalisation. In many companies, these costs were considered catch-up costs for the many decades of global expansion and growing of top-line revenue (and risk) where there had been insufficient focus on internal controls by management.

So how do we measure the benefits to be derived from improved internal control? This is especially difficult to quantify: frauds and corporate scandals which do not occur, the

"incremental" share price from the improved branding and perception of the company or the general boost to investor confidence investing in the financial markets.

Forward-looking companies have used SOX compliance as an opportunity to improve their business performance and achieve competitive advantage and greater profitability. Many companies have also used the post-SOX years to improve their business processes and especially to automate their controls globally. By better understanding the risks companies are facing, and incorporating preventive or detective monitoring controls within business processes, companies are able to be more effective and efficient in their business operations.

Effective financial controls have also been further leveraged by elevating it into a wider enterprise risk management programme. Many risks faced by companies, although initially considered to be operational in nature, invariably have a financial impact which is ultimately reported in the financial statements.

The SOX regulations continue to be fine-tuned and with the release of Auditing Standard No.5 - An Audit of Internal Control over Financial Reporting that is integrated with an Audit of Financial Statements in June 2007, companies are on the path to better achieving the correct balance of costs versus benefits.

## Guardians of corporate integrity and public interest

An AC is responsible for overseeing the financial reporting process of the company and its audits. AC members, being independent, qualified

(especially in the basic principles of financial reporting) and having the ability to ask difficult probing questions represent the guardians of public interest.

Under the 2005 Revised Code of Corporate Governance, the AC should review at least annually the adequacy of the company's internal controls (financial, operational and compliance) and risk management policies and systems established by management. The Board of Directors should comment on the adequacy of the internal controls, including financial, operational and compliance controls, and risk management policies in the company's annual report.

In my opinion, ACs empowered and ready to take appropriate action where the public interest is not protected is a wiser response than a tough regulatory approach.

## What can Singapore public companies do?

With overall improved internal control, a company is on the path to reliable financial reporting to its investors and in many cases, reduced instances of fraud.

Singapore directors, AC members and the C-Suite should think through the following questions:

- What are the main areas of risk in the company (a formal enterprise-wide risk assessment process)?
- Are there adequate internal controls in place to monitor them (documentation and regular evaluation of risks and internal controls)?
- Are there areas of potential fraud

and management override which could occur in your organisation (anti-fraud controls)?

My personal experience is that SOX and similarly detailed internal control reviews represent the greatest continuous improvement programme for companies. It should be noted that external (financial) audits are not designed to detect incidences of fraud.

I recall what Lynn Turner, a former SEC Chief Accountant, said in the early days of SOX, "You either want good internal control or you do not". ■



# The Women's Register: Matching the talents of women leaders to the needs of the community



The struggles of women have been covered extensively through the years, from the Suffrage Movement of the 1920s to the rise of feminist philosophy in the 1960s and even continues today as “a right (under the Convention on the Elimination of All Forms of Discrimination Against Women), although a few countries, mainly in the Middle East, continue to deny the right of many women to vote.”<sup>1</sup> But what can be said about the rise of women today, in both developed and emerging economies, is nothing short of phenomenal. The Economist reports that ‘...the increase in female employment in the rich world has been the main driving force of growth in the past couple of decades. Those women have contributed more to global GDP growth than have either new technology or the new giants, China and India. Add the value of housework and child-rearing, and women probably account for just over half of world output.’<sup>2</sup>

But despite the incredible progress that women have made over the years, there is still a perennial imbalance of female representation in the professional and political arenas, as well as in senior management positions. Take Singapore for example, from 1970-1984, there was no female representative in parliament with the retirement of Madam Chan Choy Siong<sup>3</sup>. Presently, Singapore has 17 female PAP elected members, 3 NMPs and 1 NCMP<sup>4</sup> but still none at Cabinet level. This under-representation occurs despite the narrowing gap in education where “younger females are as well-qualified as their male counterparts. In 2000, 81 per cent of females aged 25-34 years and 62 per cent of those aged 35-44 years had at least secondary qualifications...



corresponding proportions for the males were 82 and 64 per cent.” Under-representation is also evident in administrative and managerial, professional and technical, sales and service occupations<sup>6</sup>. While it can be acknowledged that ‘...females in Singapore have made inroads into male-dominated occupations... female representation of women in higher skilled occupations still lagged that in the developed countries.’<sup>7</sup>

Singapore is highly regarded in the global economy, a developed nation, and one that has attained first-world status yet still confronted by the empirical evidence for the disproportion of women leaders across a number of industries. The Women’s Register was thus conceived

to help address this imbalance as there was no central resource for organisations in search of women talent, particularly in those in leadership positions. This project was undertaken by the Singapore Council of Women’s Organisations (SCWO), the national coordinating body of women’s organisations in Singapore. The primary objective of the Women’s Register is to increase the level of female representation in leadership positions in the public, private and non-profit sectors. Given that women make up half of the population in Singapore, it is vital that they are encouraged to participate in the community at all levels, especially in decision-making where their actions will secure the most impact. Conversely,

organisations in these sectors can also gain access to a ready pool of female talent.

The Women's Register can best be described as a secure and confidential online facility that invites all women who consider themselves as leaders to enter their educational and professional information together with their voluntary preferences into a central database via the Women's Register website ([www.womensregister.org](http://www.womensregister.org)). It concentrates on 3 main areas, namely contribution at board level, mentoring and public speaking. It is not purely devoted to voluntary work as there are paid positions available as well. Registration is a mere S\$10 for a lifetime membership while users are given a choice between an annual membership of \$200 or a pay-per-search option. Non-profit organisations on the other hand, are charged only \$20 for an annual membership where there is no limit to the number of searches.

It was officially launched on International Women's Day on 08 March, 2007 by the Minister of State for the Ministry of Community Development, Youth and Sports (MCYS), Mrs. Yu-Foo Yee Shoon. Since then, the Women's Register has gathered more than 300 professional and senior-level women in its database and approximately 30 organisation users. MCYS has been pivotal in the success of the launch of the Women's Register, especially through the personal efforts of the Minister of State herself. Mrs Yu-Foo garnered support for the Women's Register by connecting it to the National Volunteer & Philanthropy Centre (NVPC), which in turn through their New Initiative Grant programme, administered seed

funding of S\$94,000 for the start-up of the Women's Register. This New Initiative Grant is a development fund for new and voluntary and/or philanthropic initiatives.

Apart from the opportunity to contribute to the community, women leaders can expect to receive e-newsletters that informs of new and available voluntary and paid positions as well as discounted rates or even complimentary participation in workshops, forums and seminars held by notable institutions, both local and foreign. Some past events include INSEAD's "Best of Management for Women" seminar, Self Leadership International's leadership seminars, "Strategic Leadership - Sun Tze Art of War" by Cornell Group Inc. and other workshops organised by the Singapore Institute of Management. Every quarter, the Women's Register also organises a Members' Night where members are invited to a social gathering for networking opportunities. Users that pay an annual fee are able to post on the Women's Register website for free in addition to making unlimited searches for women leaders in their respective fields. They receive free publicity for events that they organise through email blasts and their website address can also be hyperlinked from the Women's Register website.

The Women's Register will be celebrating its first birthday with its parent organisation, SCWO who are hosting International Women's Day through a Power Lunch dialogue that features top women leaders with Mrs Lim Hwee Hua, Minister of State for Finance and Transport, as its keynote speaker as well as an address by the United States Ambassador to Singapore, Ms. Patricia Herbold. This year, International Women's



Day succinctly gives tribute to the powerhousing of women in modern times, aptly themed “Women: Engines of Growth”. The audience will be able to participate and learn on how these women excelled and broke-free from gender stereotypes and the glass ceiling and managed to find the right work-life harmony at the same time. This event is open to the public and more information on the panellists can be found on the International Women’s Day website ([www.iwd.org.sg](http://www.iwd.org.sg)).

As the Women’s Register continues to grow its base and fine-tune itself, it can only mean that the populace-at-large will surely benefit from this online resource that seeks to match the talents of women leaders with the needs of the community. ■

### References:

<sup>1</sup> [http://en.wikipedia.org/wiki/Women's\\_suffrage](http://en.wikipedia.org/wiki/Women's_suffrage)

<sup>2</sup> The importance of sex, April 12th 2006, The Economist print edition

<sup>3-4</sup> Wong Aline and Leong W.K. (1993) Singapore Women: Three Decades Change. Singapore Times Academic Press. ISBN 981-210-031-8

### List of Singapore MPs

<sup>5</sup> Statistics Singapore publication - Higher Education Attainment. Last updated 30 Jun 2007

<sup>6-7</sup> Manpower Research and Statistics Department Singapore April 2000

# Non-Executive Director Remuneration - A Quick Review Of Where It Stands

## 1 Overview

Director remuneration is one of the most difficult issues to handle whether it is at the shareholders meeting or at the board meeting or outside. It is plagued by diverse interest of different stakeholders and constant questioning as to whether the director deserved the director fee he received. Whatever be the case, two things are clear: firstly, the expectations of individuals as directors have increased multi-fold and include greater time commitment, exposure to legal liability and scrutiny by the public; and secondly, regardless of the increased demands on the director, the greater his fees, the time immemorial question of whether he continues to be independent arises. But these are issues for discussion at another time.

This quick article looks specifically at directors' remuneration, focussing only on the non-executive and independent director rather than the executive director (henceforth any reference to non-executive directors will include independent directors). What the article does make clear is that it is not possible to blindly set fixed fees that non-executive directors should draw as they sit on different companies as there are simply too many variances at play. The article also stresses that given the integral role that non-executive directors play in corporate governance arrangements, the fee that is paid to the nonexecutive director must be attractive to experienced and skilled individuals. At the end of the day, it is clear that it is in the interests of all relevant stakeholders that non-executive directors are remunerated appropriately. The old ad-



By Kala Anandarajah,  
Partner,  
M/s Rajah & Tann



age that you pay peanuts you get monkeys bears reminding, particularly in this day and age, where talent is severely lacking.

Note that this article is not intended to be exhaustive but really one that provides an anecdotal review of the position across select countries.

## **2 Key Differences Between Executive And Non-Executive Fees**

By way of quick comment, as a general rule, executives are paid remuneration in consideration for their full time employment with the company. Director fees are not remuneration in the same way but rather a honourarium that is paid to directors for their contributions to the company. Whilst executive director remuneration need not be approved at a meeting of shareholders as being an expense of the company for salaries, non-executive director fees must be approved at a shareholder meeting. Typically, it is a pooled sum that is approved by the shareholders, and the board than allocates the pool amongst the non-executive directors, depending on the specific role that they play.

## **3 Are There Standard Fees Recommended That Should Be Paid**

A review of major jurisdictions shows that there is no standard recommendations as to what non-executive directors should be paid for their contributions in companies. This is because such standards are impossible to set and subjected to numerous differences that exist within a company as well as in the industry. Economic

conditions also affect what fees are to be paid from year to year. Nevertheless, what has become clear is that there is a consistent cry amongst various countries that the non-executive director is not adequately compensated. In this regard, studies have at various times been conducted by independent consultancies which suggest that non-executive directors are indeed not being compensated adequately relative to the role played and their legal responsibilities undertaken.

This despite the fact that all recent studies suggest there has been a gradual increase in non-executive director fees over the last four to five years. For example, Watson Wyatt's 2004 Executive Reward Survey indicates that non-executive director fees have risen by an average 38% per cent among FTSE 100 companies broadly. A year later, a study undertaken by a different consultancy showed that non-executive directors' fees increased twice as fast as other executives in the same year. More recent studies show that the fees have continued to increase at fairly quick rates. The position is no different in Singapore, save that there has been no study of sufficient size to provide us with definitive figures.

What is clear is that save for the trend of increasing fees, there is no consistent rate that is charged across the world.

Typically to analyse whether directors are being adequately compensated, one need only look to the quantum of time that the particular role that director is intended to undertake, the typical compensation such an individual would have drawn if the role was a fully exec-

utive one, and build in a discount for the fact that the function to be exercised is more an oversight one rather than a hands on one. This will enable a fair fee to be arrived at for a non-executive director. This is also the recommendation of the Hong Kong Institute of Directors Guide for Remunerating Independent Non-executive Directors. The Guide notes as follows:

In arriving at a rate for computing time-related INED fees, references may be made to:

- (1) How external advisers, charge clients for advice and counsel.
- (2) The average remuneration of the EDs in the company;
- (3) The average of (1) and (2), which amalgamates the above two factors and reflects proximity to market rates and in-house rates.

Indeed the Hong Kong Institute of Directors suggest that to exercise effective due diligence, it is not unreasonable for a non-executive director to devote a minimum of 100 to 120 hours per year to a company. A Watson Wyatt article titled 'The Future of Director Compensation in Hong Kong' written in the third quarter of 2006 picks this up and notes that 'total director remuneration for 100 hours of service at an hourly partner rate charges by professional advisors of HK\$4,000 should be in the range of HK\$400,000 per annum.' The article further notes that in the US, among similarly-sized companies, the annual fee paid to a non-executive director approximates this figure.

For purposes of comparison, a

Kon/Ferry-Egan Associates Study titled 2007 Board of Directors Study in Australia and New Zealand notes that non-executive directors at the top 100 companies in Australia and New Zealand are paid an average fee of A\$148,939 per year. However, within this average, there are variations and the fees can go down as low as A\$54,500. Insofar as the average fee for a FTSE 100 non-executive chairman is concerned, it is allegedly at over £250,000 a year. As regards non-executives in the FTSE 100, the average fee is allegedly over £60,000. Note that each of these fees are based on transparent calculations of the number of expected days that the individual is to spend working on the company's affairs.

It is recommended that the broad approach suggested should also be used by Singapore companies. Review the nature of the role the non-executive director is intended to perform, consider the type of individual that is required, then benchmark his fees to the number of hours he is expected to realistically spend working and reviewing the company affairs tasked to him and multiple that figure by the typical sum that an expert in his role would have charged. This is a practical and transparent approach to adopt in determining an appropriate fee to charge.

Section 4 below provides some guidance on the key factors that must be looked at when determining what a non-executive director should be paid.

#### 4 Certain Key Elements In Director Remuneration

Whilst it is not possible to recom-

mend a single remuneration structure for companies to adopt given the vagaries that exist between the different companies within a single country and across countries, it is nevertheless possible to suggest the following broad principles that companies can look to in setting their remuneration:

##### (a) Existing Policies

Consider the company's existing remuneration policies, and determine if variations need to be made to this bearing the other factors as set out below. If no revisions are necessary, then any and all remunerations should be consistently set according to the company existing remuneration policy.

##### (b) Size Of Company

Pay according to the size of the company and the level of expertise required to handle any complexity associated with such size. Typically, the larger the company, the more time an individual would be expected to spend. For one, there would be more meetings to attend, and if the individual also sat on committees, then in addition to the usual board meetings, such a person would also have to attend the committee meetings. A non-executive director who takes his role seriously would also have to ensure that he prepares in advance for these meetings. A long time experienced director who sits on the boards of a number of listed companies in Singapore says that preparation a chairman of an audit committee preparing

for an audit committee meeting should spend at least a day reading up all relevant papers, understanding the financials presented, review the risk issues, if any and ask pertinent questions. Any less time would mean that the individual may not be able to realistically fulfill the task assigned to him effectively.

As evidence that the issue of the size of the company matters is a Kon/Ferry-Egan Associates Study titled 2007 Board of Directors Study in Australia and New Zealand that shows that in in each of these two countries the average non-executive chairman fees across the 'revenue ranges from \$552,796 for those companies in the range of greater than \$10 million, to \$115,842 for those with revenue in the range of less than \$200 million'. A similar range will also be seen amongst Singapore companies broadly.

##### (c) Nature And Complexity Of Business Operations

Tied in to point (a) is the nature and complexity of the business operations. The more complex, obviously the payment must necessarily be higher. Complexity depends on the specific nature of the business, the geographic spread of the business, the nature of unusual risks associated with the business and or the company that needs to be provided for etc.

##### (d) Industry Considerations

Review the nature of the industry and consider the risk factors associated with the industry. Given the increased risk of workplace injuries associated with the construction or shipping industries, any individual appointed as a non-executive director in such an industry must ensure that he pays due heed to seeing how best to assist in directing adequate risk management. Industry considerations would also include the state of the economic conditions pertaining to the particular industry at any particular time. The idea is to benchmark fees amongst similar industries and not simply company size alone.

*(e) Qualifications Of Individual Directors*

Review the nature of the qualifications, expertise and experience the non-executive director is expected to possess when he is appointed.

*(f) Time Expended By Individual Directors*

Review the time that the non-executive director will be expected to spend in the company. Here, the approach recommended by the Hong Kong Institute of Directors is one which can work and companies should seriously consider adopting it as an approach.

*(g) Role Performed By Director*

Consider whether the non-executive director is merely sitting as a director of the board or whether he also sits on any

committees, and if so, how many and whether he chairs any of the Committees. Typically, the chairman of the company and of specific committees should be remunerated at a level that is higher than that of other directors' fees to acknowledge the additional responsibilities. See the figures provided under sub-paragraph (b) above for instance vis-à-vis a non-executive chairman and the non-executive director simpliciter.

*(h) Fee Structure*

Consider a combination of straight out fee payment and some degree of equity payment. The latter will ensure a degree of alignment between the interest of the directors and shareholders. Yet, the trick is always identifying what is the appropriate level of equity. The recommendation is to keep the percentage low. Note that this is different from providing an incentive scheme, whether through share options or otherwise, and the latter is not recommended.

*(i) Reimbursements*

Do reimburse reasonable expenses of non-executive directors, but make sure that there is clear guidance on what disbursements are claimable and how much.

fees. It is clear that whilst there has been a gradual increase in the fees that such directors draw, there has been no consistent approach across the world. It is also not evident that a similar increase, or at least rate of increase as in some other countries, has been observed in Singapore. However, given the talent shortage, it is necessary for a long and arduous look to be given to the state of non-executive director fees and bring it in line with market forces. The approach of benchmarking salaries not just against that of other directors in comparable companies, industries and other countries, but also against what a full time consultant would have charged on a per hour basis and then working in a discount is much to be lauded and should be adopted. Stakeholders should recognise that without appropriately qualified individuals who will spend the time and dedication, it is the company and eventually the other stakeholders who will suffer. ■

**5 Conclusion**

As noted, this article was intended to provide a quick overview of the state of non-executive director

# Between a Rock and a Hard Place

## The CPF Paradox

By David Sandison, Tax Partner, PricewaterhouseCoopers



To strengthen and enhance the social safety net for Singapore citizens, the Government has, over the past few years, been fine-tuning the tax treatment of Central Provident Fund (CPF) contributions. This has included raising the employer's CPF rate by 1.5% from 13% from 1 July 2007, introducing a workfare scheme for low-wage workers, modifying the CPF system to complement this scheme, and increasing the limit or expanding the scope of deductions for CPF top ups. This is to name but a few of the measures taken.

All these changes have been made with a view to encouraging Singaporeans to save for retirement. Unfortunately though, in striving to achieve social stability in Singapore, the Government has overlooked a select group of individuals, that is, those who take on roles as non-executive, or independent, directors of local companies ("NEDs"). These stalwarts seem to have fallen between two stools; and I don't mean at the Cricket Club bar.

The difficulty appears to stem from the fact that NEDs are not employees; they have no contract of employment. In addition, the CPF Board does not regard them as carrying on a trade, business, profession or vocation. In most cases therefore, they are unable to contribute to the CPF at all. If for some reason they do make contributions, and these are accepted by the CPF, then they are voluntary contributions, which you would naturally think must somehow qualify for tax relief along with contributions made by the rest of the population.

Enter the income tax problem. There are only two ways that a person can get tax relief for his CPF contributions. The first is under section 39(2)(g) of the Income Tax Act ("ITA"). Relief is only available here however, where the contributions are obligatory by reason of a contract of employment, or by reason of the rules or constitution of the CPF.

Not surprisingly, as a NED will not have a contract of employment in the first place, there can be no

contractual obligation; and as he is not, in fact, an employee, he is not obliged under the CPF Act to make contributions. Exit option one.

The second way is under section 39(2)(h) which covers a person carrying on a trade, business, profession or vocation. Deductions, up to certain limits, are given for contributions made "on his own account", in other words, voluntarily. "There is your answer", you might be tempted to think. You would be a little wide of the mark.

The problem here arises from a throw away amendment to the ITA in 1993 that was designed to ensure that NEDs were taxed in the same way as any other employee and could not get out of paying tax on benefits in kind and the like. The amendment quite simply and innocently changed the definition of "employee" to include directors of a company. As section 39(2)(h) only applies to, effectively, the self-employed, then NEDs fell outside the definition. Their only recourse then was to section 39(2)(g), which of course we have seen they are excluded from also.

This rather sad and inequitable state of affairs was pointed out to the Ministry of Finance ("MOF") by the Singapore Institute of Directors ("SID") in May this year. The response was, somewhat, disappointing. Essentially it confirmed that all this had been done as part of "policy" to exclude NEDs who could otherwise have "an exclusive advantage" as they could then "decide their own preferred amount of CPF contributions each month and get full exemption on that amount".

It is difficult to see what this exclusive advantage could be. The otherwise happily self employed can decide their own preferred amount of CPF contributions (up to specified limits), provided they have at least put away the mandatory Medisave contribution. So there should be no difference with NEDs. The only consolation, apparently, is that NEDs do not have to make Medisave contributions!

It is clear that this is an unfair situation as it cannot be part of any sensible policy intention to exclude a minority group of people who, after all, are carrying on a business, profession or vocation in taking on these roles, just like any other sole trader selling chick

blinds or fixing your plumbing; and it is contrary to the general aim of ensuring Singaporeans can put something aside for old age.

I think that there are two things that need to be done. The first is to rectify the situation with the CPF Board and get them to confirm/accept,



that NEDs qualify as any other member of the self employed community to make voluntary contributions (and of course, mandatory Medisave contributions). The second is to persuade the MOF to amend the legislation again. This would simply mean moving the definition of employee from the general definitions section (which means it applies throughout the ITA), to section 10, which taxes "gains or profits from any employment". All that then would be needed would be to insert a limitation on scope by saying: "For the purposes of this section only, employee includes....". That then allows section 39(2)(h) to rescue the situation.

Nobody has any objection to NEDs paying tax on their perks and benefits. That is only fair; but NEDs must, I am sure, object to being left lying between two stools, metaphorically speaking. ■

# SID's 9th AGM and Annual Luncheon

The Singapore Institute of Directors held its 9<sup>th</sup> Annual General Meeting on Tuesday 13 November 2007 at Raffles Hotel, Singapore.

The Annual General Meeting (AGM) was attended by about 40 members. At the AGM, Mr Adrian Chan Pengee, Mrs Fang Ai Lian, Ms Kala Anandaraman, Ms Yeo Lian Sim and Mr Yeoh Oon Jin were re-elected to the Governing Council. Dr Ahmad Mohd Magad, a member appointed to the Council during the year, was elected to the Governing Council.

Immediately after the AGM, the Institute held its Annual Luncheon. The Guest-of-Honour for the Annual Luncheon was Mr Lim Boon Heng, Minister, Prime Minister's Office. About 250 members and guests were at the luncheon.

SID thanks Mr Lim Boon Heng for being the Guest-of-Honour and all distinguished guests and members for attending the Annual Luncheon. It also wishes to record its appreciation to the many individuals and companies that booked tables to make the annual event a success. ■





## Speech by Mr Chew Heng Ching, Chairman of Singapore Institute of Directors at the Institute's 9<sup>th</sup> AGM Luncheon on 13 November 2007



Mr Lim Boon Heng, Minister in the Prime Minister's office, Distinguished Guests, Members of SID, Ladies & Gentlemen. Welcome to the SID's 9th AGM Luncheon.

As the Institute celebrates its 9<sup>th</sup> anniversary, I would like to take this opportunity to once again thank all members, my fellow Council members, past and present, and the corporate community for the support and encouragement given to the Institute since its formation in 1998.

We have come a long way since the difficult days during the Asian financial crisis. Today, Singapore's corporate governance standards are among the best in Asia. If we are to retain our pre-eminent position, much more still needs to be done to continuously raise the level of awareness and standard of best practices in the governance of our companies. It is work-in-progress. And it is work by the many public agencies and professional institutes

(including SID) and investor associations dedicated to promoting excellence in corporate governance in Singapore.

Directors' training is an important part of good corporate governance. It is important that directors receive adequate training to assist them in carrying out their duties. Training is especially important for new or first-time directors so as to equip them in understanding their roles and responsibilities, and with the necessary skills. Even experienced directors need to continually upgrade their skills and knowledge, in order for them to guide their companies in this rapidly changing global landscape.

In this connection, members would have read about the Institute and the Monetary Authority of Singapore (MAS) commissioning a consultant to conduct a Strategic Review on how SID can play a greater role in further improving corporate governance

here. In particular, the Review will look at how to build on the useful work by SID and develop a comprehensive and sustained approach to training and development of directors in Singapore. It will also look into the resources required by the Institute to carry out this enhanced role. (As you probably know, SID till now has been run by volunteers supported by a small secretariat. This will have to be strengthened including the employment of a full-time CEO if SID is to assume the enhanced role). The Review will also examine developments in corporate governance globally and best practices of similar institutions in major jurisdictions. The Strategic Review is expected to be completed in the first quarter of 2008.

On behalf of the Council, I am pleased to report that the past year had again been a busy one for the Institute. We held many talks, seminars, workshops and other events for the benefit of members. We continued to provide training for directors and would-be directors on their role as members of boards, be they executive or non-executive independent directors. I am glad to report that our courses and events have been well attended.

One of the most successful programmes was a series of seminars conducted in collaboration with The Singapore Exchange (SGX) in



both English and Mandarin, entitled "Understanding the Regulatory Environment in Singapore" for listed company directors and senior managers. More than 700 participants attended the 10 sessions (8 English and 2 Mandarin) held during the last 12 months.



A first was also achieved when a certificate programme in directorship was launched in July 2007 in partnership with the Singapore Management University. Successful completion of the 3 module programme will lead to a certificate in directorship. So far 2 modules have been conducted and very positive feedback has been received. There are plans to introduce a diploma programme in directorship in 2008/9 for those who have completed the certificate level programme.

A series of finance and law related workshops was also conducted. Such workshops, often using real case studies, served to provide directors with relevant and useful practical experience on key issues and challenges confronting them in their role.

Earlier this year, we successfully concluded the third run of the Best Managed Boards Award and held the inaugural CEO of the Year Award. These two awards were organised as part of the annual Singapore Corporate Awards.

On membership of the Institute, our number has reached the 1,400 level. Each year we were able to sign on a good number of new members but at the same time some choose to leave the Institute following their retirement. To cater to the varying needs of members, the Institute will continuously explore how best

to meet those needs and strive to offer even more benefits and value to members.

Each year, we consciously make the effort to renew the Council by bringing in one or two new faces while some leave after having served a good number of years at the Council. The Council has expanded steadily over the years and we now have 17 members. At today's AGM, a new member, Dr Ahmad Mohd Magad, was elected to the Council.

I would like to thank each and every one of the Council members for having so graciously and selflessly served the Institute over the years. We look forward to their future contributions and also hope to have their continued support for all our activities.

I must also mention that many members have also come forward to serve on the various sub-committees formed by the Institute to focus on different aspects of its activities. Some sub-committee members are relatively new while others have served many years and I wish to thank all of them.

With much regret, I report the untimely demise of our long time Honorary Fellow, Mr Sim Kee Boon. I wish to place on record the Institute's appreciation to the late Mr Sim for his constant encouragement and guidance given to the Institute over

the years.

I must say that the Institute would not be where it is today without the strong support of the local corporate community, including the professionals such as lawyers and accountants. The corporate community had always been very supportive of our efforts and activities and had willingly offered their services gratis whenever called upon.

Though I would much like to mention all these corporate supporters by name, I am wary that I might inadvertently omit some of them. For that reason, I will only mention names of those who partnered the Institute in organising some events during the past year - they are SGX, Egon Zehnder, Hewitt, KPMG, PwC, SMU and Wong Partnership.

Finally, I also thank our corporate sponsors for their contributions and continued support of the Institute. And also all members of the Institute who have in their own ways contributed to the efforts of the Institute in its mission of raising the standard of corporate governance in Singapore. And last, but certainly not least, I thank our Distinguished Guest of Honour, Minister Lim Boon Heng for taking time off from his busy schedule to grace this occasion.

Thank you and have a pleasant luncheon. ■

# SID 7<sup>th</sup> Annual Golf Tournament



SID held its 7<sup>th</sup> Annual Golf Tournament on Sunday 16 September 2007 at the Tanjong Course of Sentosa Golf Club. The Guest-of-Honour for the event was Mr S Iswaran, Minister of State for Trade & Industry. The tournament, which started at 1.00pm, was participated by 128 members, guests and well-wishers.

A post-tournament dinner was held in the evening, immediately after the tournament ended. It was very well attended with most participants, including the Guest-of-Honour and other VIPs, staying back for the presentation of prizes to the winners of the various categories and the lucky draw.

The tournament was organised by Mr David Wong See Hong (as chairman), Messrs Chew Heng Ching, John Lim Kok Min, Boon Yoon Chiang, Giam Chin Toon, Lim Hock San and Mrs Yvonne Goh.

SID thanks all sponsors, donors, participants, the SID golf tournament organising committee, Sentosa Golf Club and all who had assisted in the successful completion of the tournament. ■





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# RESULTS OF SID 7<sup>th</sup> ANNUAL GOLF TOURNAMENT

### OVERALL WINNER

Tan Yam Pin

### A DIVISION (HANDICAP 0-18)

Winner:	Richard Ng
1st Runner-up	Richard Chee
2nd Runner-up	Lim Swee Kwang
3rd Runner-up	Eddie Chow

### B DIVISION (HANDICAP 19-36)

Winner:	Adeline Ting
1st Runner-up	Ted Lau
2nd Runner-up	Lam Kun Kin
3rd Runner-up	Chew Hai Chwee

# Seminar on Foreign Exchange Exposure

A half-day seminar on Foreign Exchange Exposure, covering topics such as "Understanding Financial Instruments", "Understanding and Managing Risks and Control" and "Understanding Legal Risks", was held at Orchard Hotel Singapore on 27 November 2007. The seminar was jointly organised by SGX, SID and KPMG. Response was very good and it was attended by about 170 participants.

The speakers were Mr Ong Pang Thye and Mr Irving Low from KPMG, Mr Udi Epstein from Deutsche Bank and Mr Dilhan Pillay Sandrasegera from WongPartnership. A panel discussion was held towards the end of the seminar. Joining the speakers for the panel session was Mr Tang Yuen Ying of SGX.

SID thanks the speakers and panellists for their kind contribution and SGX and KPMG for co-organising the seminar with SID. ■





## Events Calendar

### SID-SMU Executive Certificate in Directorship

#### *Executive Skills for Board Members in Challenging Times*

SID and the Singapore Management University (SMU) offer a certificate-level program in business and governance for company directors and would-be directors. Upon successful completion of the certificate-level program, participants will be eligible to proceed to attend a diploma-level program leading to an Executive Diploma in Directorship.

The certificate-level program comprises three modules, each of three-day duration and conducted in consecutive blocks of 1.5 day sessions spread over 2 weeks. Assessments will be conducted a week after the completion of each module. Participants need to complete all 3 certificate-level modules to be awarded the Executive Certificate in Directorship.

#### **Module 1**

The Role of Directors: Duties, Responsibilities and Legal Obligations  
3-4 April 2008  
10-11 April 2008  
18 April 2008 (Exam)

#### **Module 2**

Strategic Business Directions  
(Dates to be advised)

#### **Module 3**

Finance for Directors  
7-8 May 2008  
15-16 May 2008  
23 May 2008 (Exam)

*For more information and registration, please contact:*

*Ms Karen Yeo  
Tel. 6828 0287  
karenyeo@smu.edu.sg*

*Ms Esther Tan  
Tel. 6828 086  
esthertan@smu.edu.sg*

*Ms Rachel Tan  
Tel. 6828 0375  
racheltan@smu.edu.sg*

*at the Office of Executive Education, Singapore Management University (SMU). You may also contact SID Secretariat at Tel. No. 6227 2838 for any enquiries.*

### SGX Listed Companies Development Programme: "Understanding the Regulatory Environment in Singapore"

This one-day programme is co-organised by SGX and SID. The programme is specially designed for directors and senior management of SGX-listed companies and companies aspiring to a listing on SGX. The topics covered and the presenters are:

"Directors' Duties and Responsibilities" by Ms Kala Anandarajah, Partner of Rajah & Tann and Council Member of SID

"Risk Management and Internal Control" by Mr Ng Siew Quan, Partner of PricewaterhouseCoopers

"Corporate Governance and SGX's Regulations" by Mrs Yvonne Goh, Managing Director of KCS Corporate Services Pte Ltd and Council Member of SID

The date for the next programme is: Thursday 29 May 2008

*For more information, please contact SID Secretariat at Tel. No. 6227 2838*

# WELCOME ONBOARD

## SEPTEMBER 2007

Chan Meow Khing Jeanna	Lim Andy
Chan Wai Meng Charles	Ng Chee Tiong
Cheah Yee Ping Angelic	Tan Beng Hwee Andrew
Grundlingh Johan	Yeap Lam Yang
Lee Soon On	

## OCTOBER 2007

Cheong Fook Onn Andrew  
Chim Suan Kit Mark  
Eng Siang Cher Patricia  
Foo Moo Tan Peter  
Gin Hoey Kwan Hoong Kevin  
Goh Mong Song

## JANUARY 2008

Ansari Khawaja Raza Mohmood	Law Kok Kheng Wayne	Rajan Nagarajan
Bowman William Sefton	Lee Kok Wah	See Chak Mun
Chan Mui Chin Angela	Lee Kwang Mong	Siu Yeung Sau Sean
Chin Jin Meng	Lim Wah Liang William	Soh Choon Min
Cronin David	Low Christopher	Stead Robert Henry
Dutt Subhangshu	Low Siew Sie Bob	Tan Eng Ann
Fong Teck Loon Jimmy	Luk Wai Lun Alan	Tan Ngee Teck
Garner Martin	Na Boon Chong	Tay Joo Soon
Goh Cheng Keow Theresa	Nathan Shashidran	Ting Sii Tien Philip
Karyeo Abdul Rashid	Ng Chee Sin	Ventura Alain
Koh Kok Leong Gary	Ong Tian Khiam	Wong Kum Ying
Koh Yee Luang	Ong Wai Chong	Yaw Chee Siew

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