Corporate Governance In Singapore

An Asian Business Environment

CORPORATE GOVERNANCE REDEFINED

The need for corporate governance was first mooted by Berle and Means in their classic 1932 work on *The Modern Corporation and Private Property*. Their analysis was that control of the corporation has passed irreversibly from the owners, the shareholders, and is vested in the directors and managers who enjoy managerial autonomy. Corporate governance becomes an issue because of the separation of ownership and control.

The Cadbury Report noted that corporate governance is concerned with the way in which companies are directed and controlled. This indeed is the crux of the issue : with each individual portfolio investor typically owning an inconsequential stake in a publicly-listed company, no one shareholder can exercise effective control of a corporation.

Portfolio investors have little incentive to monitor management; if unhappy the investor can exit the company by selling his shares. The Singapore Corporate Governance Committee ("CG Committee") noted that "Corporate governance refers to the processes and structure by which the business and affairs of the company are directed and managed, in order to enhance long term shareholder value ….." It went on to say that good corporate governance therefore embodies both enterprise (performance) and accountability (conformance).

There is probably no doubt that good corporate governance enhances corporate performance and that in turn increases shareholder value. In a June 2000 McKinsey survey, 77 percent of the respondents in Asia ranked board practices to be at least as important as financial issues in stock selection.

With respect, the emphasis on the economic benefits of corporate governance arguably misses the point. In the writer's opinion, *the central issue of corporate governance is the accountability of management, the most critical of which is managing the transparency and integrity of any situation in the company where there is or will be a potential or actual conflict of interest.*

Whether a corporation performs profitably or makes enormous losses is a matter for the business judgement of the board of directors. Indeed, high standards of corporate governance may not necessarily lead to exceptional company performance. Many other factors may influence company performance. It would be reasonable to assume that bad corporate governance will not deliver enduring company performance.

Corporate transparency issues can arise in all situations regardless of company performance. This was the case with Enron and Worldcom in the United States where the directors have previously announced extraordinary profits.

Corporate governance is an issue even if there is no complete separation of ownership and control. Indeed, it is over-simplistic to assume that there is necessarily a complete separation of ownership and control in large companies. In the Asian business environment, the founders or family controlling shareholders will retain a significant percentage of the listed company's shares after it has gone public.

To maintain a public listing the Singapore Stock Exchange requires a minimum free float of at least 10 percent of the shares in issue to be held by shareholders who are unconnected members of the public. The controlling shareholders' dominance is exerted through informal influences beyond the board of directors.

As a result there is no obvious external accountability and transparency in decisions where vested interests are at stake. Self-dealings by the controlling families take the form of loans to shareholders, transactions with related parties, loans to directors who are family members, and trading with related parties at less than arms-length basis.

S Y N O P S I S

The purpose of this paper is to examine the development of the corporate governance regime in Singapore in an Asian business environment.

This paper will examine in detail the present corporate governance regime in Singapore. This will include the Singapore Code of Corporate Governance and the Singapore Stock Exchange or SGX Listing Manual disclosure obligations.

The focus of the paper will be on how the Singapore corporate governance regime addresses the issue of accountability of management and conflicts of interest situations. These will include the independence of directors, interests of directors in transactions where they will benefit either personally or as substantial shareholders, and the employment of relatives of directors or shareholders in managerial positions. It is also important to ask : how "independent" are the independent directors?

In view of the concentrated family shareholdings of most Singapore listed companies, a primary focus of this paper will be on the fiduciary duties of directors, particularly in situations where there is a conflict of interest. A portfolio investor who has very little voting power will have to rely on the directors as the most important corporate governance guardian on behalf of the company.

Even in situations where there is no apparent conflict of interest, the Singapore director who comes from the controlling shareholders will have to recognise his common law duty to the interests of the company, and at times, to the rights of minority shareholders. It is settled law that, with some exceptions, a director owes a fiduciary duty of care to the company but not to the individual shareholder. A director is an agent only of the company and not of the shareholders.

Company law is the foundation for corporate governance. The paper will therefore consider the duties of directors under the Companies Act and under the common law. In particular, the paper will state the important equitable and common law principles on directors' duties and refer to leading Singapore and common law cases on these principles. It will address the issue of the accountability of directors - to whom are directors' duties owed? The paper will also look at the rights of minority shareholders.

The paper will consider how Singapore can be expected to respond to the need to maintain internationally accepted standards of corporate governance in an Asian business environment. It will comment on how proposed changes to the SGX Listing Rules, the coming into force of the Securities and Futures Act, and the proposed changes to company law from the Singapore Company Legislation and Regulatory Framework Committee, will impact on the corporate governance regime.

The paper will conclude, in the light of the accounting and corporate scandals coming out of the United States, that there is no one single model of corporate governance to follow, for a country or a company. Over time, there may be a convergence to internationally accepted standards of corporate governance.

CONCLUSION

In conclusion, corporate governance in an Asian business environment requires a fine balance between governance and performance. Tight corporate governance rules increase business costs significantly. Beyond the cost issue, the debate is whether tighter corporate governance rules will actually stifle corporate performance.

Whilst there is an obvious conflict of interest in having controlling shareholders dominate the board, there is an argument that controlling shareholders keep the pressure on directors and senior management to maintain the impetus and drive for better corporate performance. In other words, the board would have to deliver profits and dividends to the company. Although this is an attractive argument, there are no empirical studies in Singapore to determine that family-controlled listed companies do perform better financially than companies which have diffuse and diverse portfolio investors.

In the writer's view, what is important is not necessarily the tightening of corporate governance rules but the existence of a corporate culture of board practices and control measures that can identify, monitor and manage conflict of interest situations.

The United States introduced drastic measures in the wake of the accounting scandals and the massive bankruptcies first of Enron, followed by Worldcom and other corporations. The Sarbanes-Oxley Act of 2002 which became law on 30 July 2002 requires that the audit committee should comprise of only independent directors.

It increases the maximum prison sentence to 25 years for any person engaging in any scheme or artifice to defraud investors. It gave corporations six months from 30 July 2002 to set up a Code of Ethics for senior financial officers. In addition, it requires the chief executive officer and the chief financial officer to certify the corporation's annual and quarterly reports fairly represent the financial condition of the corporation.

In the writer's opinion, the corporate scandals in the United States came about in an environment that combines a voluntary corporate governance regime with the lucrative monetary incentives, running into hundreds of millions of dollars, in bonuses and stock options for senior executives who meet profit targets.

In the case of Enron, it took only one-hour of teleconferencing with its 18 member board in 1999 to approve the dubious LJM deals which created more than half of the US$1 billion in losses in 2001. The 18 member board had distinguished independent directors such as Lord Wakeham, the former British energy secretary.

At the beginning of this paper we refer to Berle and Means' thesis that corporate governance is an issue because directors and managers enjoy managerial autonomy from shareholders. This is certainly the case with Enron and Worldcom where there are no controlling family shareholders who exercise significant influence over the board.

Indeed this state of affairs should be a salutary reminder that there is no conclusive evidence that any one model of corporate governance leads to superior corporate performance. Rather corporate governance standards will converge over time to internationally accepted standards to meet the needs of the global investment markets.

This is not the full LLM Paper.
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