4 April 2018

The Secretariat, Corporate Governance Council
c/o Markets Policy and Infrastructure Department
Monetary Authority of Singapore
10 Shenton Way, MAS Building
Singapore 079117

By email to: MAS_MCP@mas.gov.sg

Consultation Paper on Recommendations of the Corporate Governance Council (Revised Singapore Code of Corporate Governance)

Dear Sir,

The Asian Corporate Governance Association (ACGA) welcomes the opportunity to comment on the consultation paper regarding amendments to the Singapore Code of Corporate Governance and related revisions to the Listing Rules.

ACGA is a not-for-profit membership association chartered under the laws of Hong Kong and founded in 1999. The Association is dedicated to working in a constructive manner with regulators, listed companies and investors across Asia to improve corporate governance standards and practices, which we believe are a foundation for long-term economic development. We are guided by a practical, long-term approach that is relevant to each individual market. Our operations are supported by a membership base of institutional investors, Asian listed companies, insurance and accounting firms, and universities. ACGA has more than 110 corporate members, two thirds of which are institutional investors with more than US$30 trillion in assets under management globally. They are also significant investors in the Singapore market.

High-level comment

We very much welcome the spirit of the proposed amendments, namely to reinforce the core principles of corporate governance, remove out-of-date guidelines, and elevate some fundamental provisions to the Listing Rules. We also believe that restating the meaning and purpose of the "comply or explain" concept is timely, as we would agree that a compliance mindset has emerged among many, though not all, listed companies.

We are concerned, however, by the proposal to separate the current Code into a shorter principles-based document and a new Practice Guidance. Some elements being moved to the

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Guidance should be in the Code, in our view, while the voluntary nature of the Guidance document could relegate it to second-class status in the eyes of many issuers. We also have doubts about the new language relating to "comply or explain" in the Code and whether it will achieve its objective of changing the current compliance mindset.

Our specific responses to each question follow:

Question 1: Draft introduction to the Code

The draft Introduction provides a strong and clear statement on the value of corporate governance to companies, and the importance of balancing shareholder and stakeholder needs and interests. We particularly like the emphasis on the leadership role of the chairman in setting the tone and encouraging a "full and frank exchange of views" in the boardroom. Despite being critical for board effectiveness, this aspect of governance often receives less attention than it deserves.

We have questions, however, as to whether the new Comply or Explain section following the Introduction will achieve its intended purpose. It states for example:

> "Companies are expected to comply with the Provisions of the Code, and variations from Provisions are acceptable to the extent that companies explicitly state and explain how their practices are consistent with the aim and philosophy of the Principle in question. The explanations for variations should be comprehensive and meaningful." (*underlining added*)

It is probable that many issuers will take this to mean compliance is compulsory.

Alternative wording that allows companies to adapt to the spirit of the Code could be as follows:

> "Companies are encouraged to apply the Provisions of the Code after careful consideration and board discussion. Automatic compliance or "box-ticking" is discouraged. Companies may choose not to apply any Provision which they believe will bring only limited improvement to their governance practices. They are however required to explain in meaningful detail how their practice is consistent with the aim and philosophy of the Principle in question."

The standard for "meaningful" should not be simply what management considers meaningful, but what independent shareholders and stakeholders consider informative and useful.

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Question 2: Streamlining the Code

With certain important caveats, as outlined below, we broadly support the streamlining of the current CG Code and the plan to move 12 Provisions (currently called Guidelines) to the Listing Rules of the Singapore Exchange.

Regarding the 15 Provisions (Guidelines) that are to be removed from the Code either because they replicate changes that have already taken place to the Listing Rules (hence are redundant) or because they are "overly prescriptive": We support removing the redundant parts of the Code, such as earlier guidelines on voting by poll, the two-proxy rule and continuous disclosure of material events. However, it is debatable whether the other Provisions should all be classified as too prescriptive. Encouraging companies, for example, to write a formal letter to each new director setting out his or her duties and obligations is an excellent practice that helps to strengthen board governance. It not only shows a degree of professionalism in board management, but provides clear guidance to new directors of what is expected of them.

Regarding the 24 Provisions (Guidelines) to be shifted to the new Practice Guidance document, our comments are under Question 3 below.

Question 3: The new Practice Guidance

Some elements of the Guidance lend themselves to being in a non-binding document of this nature, such as general descriptions of the board's role, how non-executive directors should behave, and the evaluation process for individual directors. However, as we note below, we are not in favour of splitting the definition of "independent director" between the Listing Rules and the Practice Guidance. Moreover, some provisions moved to the Guidance are too important not to be in the Code or Listing Rules. For example:

- Avoiding the appointment of alternate directors.
- Defining the role of the company secretary.
- Detailed disclosure guidelines for director and senior executive remuneration.
- The right of the Audit Committee to have additional resources to do its job properly and a duty to review the breakdown of fees paid to the auditor for audit and any non-audit services.

Indeed, making many of these provisions voluntary would appear to represent a material reduction in governance standards for listed companies in Singapore.

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Question 4: Rationalising tests of director independence

We strongly disagree with splitting the criteria for director independence between mandatory Listing Rules and voluntary provisions in the Practice Guidance.

The proposal envisages moving certain "objective and baseline" tests for director independence from the current Code to the Listing Rules, while moving the remaining tests to the Practice Guidance. This means that the following criteria for non-independence will now be in the Rules:

- A director who was employed by the company or its related corporations for the current or any of the past three financial years;
- A director whose family member was employed by the company or its related corporations for the current or any of the past three financial years;
- A director who is, or has an immediate family member who is, a substantial shareholder of the company;
- A director who has served on the board for more than nine years.

Meanwhile, criteria relating to people with significant business relationships with an issuer in the recent past will be put in the Guidance:

- A director who, or whose immediate family member, in the current or immediate past financial year, provided to or received from the company or any of its subsidiaries any significant payments or material services;
- A director who, or whose immediate family member, in the current or immediate past financial year, is or was a substantial shareholder, partner, executive officer or director of any organisation which provided to or received from the company or any of its subsidiaries any significant payments or material services;
- A director who is or has been directly associated with a substantial shareholder of the company in the current or immediate past financial year.

The stated aim is to "provide companies with flexibility". On the contrary, it may create confusion in the minds of companies as to who can or cannot be considered independent. It will almost certainly cause confusion among international investors, since the items listed as being of secondary importance form a core part of the definition of independent director in most markets around the region. It would be more credible to include all the tests of director independence in one place—the Listing Rules.

We also recommend that the cooling-off period of three years for former executives and one year for people with business relationships is far too short and should be reviewed. Indeed, it is questionable whether cooling-off periods are effective in the context of the concentrated ownership prevalent in Asia.

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Question 5: Lowering the threshold for assessing director independence

We disagree with the proposal to lower the shareholding threshold for assessing director independence from 10% to 5%. That is, any director who is connected to a "substantial shareholder" owning 5% or more of the issuer would be considered non-independent. While the paper notes that such a bright-line test is in line with definitions of substantial shareholder in Singapore company and securities law, as well as rules in Hong Kong and Australia, it creates two main problems in our view:

1. That a director nominated by a shareholder with a 4.99% stake would be considered independent, while one nominated by a 5% shareholder would not be. This would be counterproductive.

2. That genuinely independent institutional investors with stakes of 5% or more would be disenfranchised from nominating candidates for independent director. This leads to the following contradiction: people nominated by funds with no connection to a controlling shareholder are considered not to be independent, while those nominated by a board controlled by a family or state owner are considered independent.

This rule does not fully account for the way in which capital markets have evolved over the past decade, namely the emergence of substantial institutional shareholders which have no ties to controlling shareholders. Nor does it take into account the impact on director independence of different ownership structures: while a 5% holding in a dispersed-shareholding company in Australia could create real conflicts of interest for director independence, the same will not necessarily apply in Asia where most listed companies have a controlling shareholder.

Our view is that the current threshold of 10% is more likely to be appropriate. However, before a final decision is made it would be useful for SGX to undertake a survey of ownership structures in Singapore in order to ascertain the prevalence of independent institutions owning more than 10% of listed companies.

We also wish to note an apparent contradiction in the revised Code between this substantial shareholder rule and the two-tier vote process. Namely, it is proposed that a shareholder with a 5% stake cannot nominate an independent director, yet would be classified as part of the independent or "non-controlling" shareholder body for the purposes of two-tier voting (since the threshold for "non-controlling" is anyone owning less than 15% of a company).

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Question 6: New nine-year rule on director independence
The consultation proposes a stricter approach to independent directors who have served for nine years or more. Instead of continuing with the current recommendation for a rigorous review of their independence, the Code suggests two new options: a hard limit of nine years for any independent director or a requirement for a UK-style "two-tier vote" on any independent director who wishes to serve more than nine years.

While there is merit in both approaches, we favour a hard limit of nine years. Our reasoning is closely aligned with the rationale given in the consultation paper:

- A hard limit would facilitate greater board rejuvenation. This is clearly needed in many listed companies in Singapore—as the paper notes, almost 30% of independent directors serve more than nine years and some for several decades.
- A hard limit would likely facilitate greater board diversity.
- A hard limit would not bar valuable independent directors from remaining on a board as non-executive directors.

In addition, imposing a limit would create demand for more independent directors, thereby expanding the available pool.

Two-tier vote from year 1
We also see merit in applying a two-tier voting process to all independent directors from the outset. This would add credibility to their election and position as it would engender greater trust in the nomination and election process among minority shareholders. Indeed, the two-tier system was introduced in the UK precisely to address the governance problems of controlled companies and applies for all appointments regardless of tenure, as the consultation paper notes. Since the controlled company issue is far more pertinent in Singapore and other parts of Asia, there seems no sound reason why minority shareholders should have to wait nine years to exercise the same rights.

Questions 7-8: Disclosure of non-controlling shareholder votes on independent directors
We agree with the proposal that companies should disclose the voting split between controlling and non-controlling shareholders on independent directors who have served less than nine years. Indeed, it would be a welcome reform if such a voting breakdown was given for all director votes and other resolutions, as is already the case for companies listed in India.

Regarding operational issues that could arise from such separate disclosure, one factor could be the difficulty of ascertaining in certain circumstances whether all shares held under nominee companies were indeed independent. The same challenge could apply for any two-tier voting system being introduced.

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Questions 9-10: Proportion of independent directors
We agree with shifting the one-third minimum requirement for board independence from the Code to the Listing Rules.

We broadly agree that a majority of the board should comprise independent directors if the chairman is non-independent.

However, quantity is not all. We believe the Code and Listing Rules could do more to require companies to disclose the specific reasons for nominating any person as a director, not just general biographical details as envisaged in Guideline 4.7 (which is being moved into the Listing Rules). This would include any unique skill sets that will complement the knowledge and expertise of other directors.

We also have some related concerns:

1. Given our disagreement with splitting the definition of "independent director" between the Listing Rules and Practice Guidance, and the short to very short cooling-off periods envisaged in both documents for candidates with some relationship to the company, it is highly likely that people with close business connections will be eligible to become independent directors. This will undermine the spirit of the Code and the value of proposals to increase the proportion of independent directors.
2. The one-third minimum requirement is intended as a floor, but may become a ceiling for many issuers. It is critical that companies are encouraged to expand the independent component on their boards as their needs and businesses change. One-third may be appropriate for a local company with a simple business. It will most likely not be adequate for a complex regional or international firm with three to five board committees.
3. While we agree in spirit with the majority independence proposal above, there is the possibility that this will leave some companies without a sufficient number of directors who understand their business. This could either weaken board decision-making or allow a dominant chairman even more control.

Question 11: New provision on management and business relationships
We broadly agree that a majority of the board should comprise directors who have no management or business relationship with the company, as long as this does not weaken the board in any material way.

Question 12: Board diversity
We support the proposal for companies to disclose their board diversity policies and progress in achieving them. We recommend that the concept of the "board skills matrix" be included in the Practicing Guidance.

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Question 13: Remuneration
We were disappointed to see that the Council decided against introducing a "say on pay" advisory vote for the time being, and instead emphasised that the provision meaningful disclosure on remuneration was more important. Yet these two things are not mutually exclusive.

One of the benefits of a "say on pay" vote in markets outside the region, such as Australia, has been its positive impact on company-investor dialogue on a broad range of governance issues. This is an area where Singapore could take the lead in the region.

Question 14: Stakeholder engagement
The proposals for enhanced shareholder and stakeholder engagement could be considerably strengthened. For shareholders, there is no mention of the concept of "stewardship" and how the relationship between companies and their minority shareholders is changing. There is also no guidance on how directors should respond to institutional investors seeking to implement their stewardship responsibilities. While the Singapore stewardship guidelines are a voluntary set of principles, not a "comply or explain" code per se, many foreign institutional investors are now operating under "comply or explain" codes from their home country or in other parts of Asia. It is unlikely they would not seek to apply the same engagement approaches in Singapore as they do elsewhere.

The section on stakeholder engagement, meanwhile, is extremely terse and makes no mention of key issues such as sustainability or the environment. Indeed, there is no mention of how the new Code links to the SGX Sustainability Reporting Guide of June 2016. There are brief mentions of sustainability in the Practice Guidance, but these refer to the company and not to external sustainable development concepts. A greater emphasis on these issues would underline their growing importance to companies, investors and the wider stakeholder ecosystem. Environmental and social issues are material and will play a larger part in how companies are valued and perform in future.

Question 15: Comply or explain
Our views on this are covered under Question 1 above.

Question 16: Corporate Governance Advisory Committee
We support the proposal to establish a standing committee with the remit of keeping the Code and Practicing Guidance up to date. To have broad market credibility, such a committee should have adequate representation of investors (institutional and retail) in addition to issuers and related intermediaries.

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Question 17: Proposed Listing Rule Amendments
We have no further comments on the proposed Listing Rule amendments beyond what we have expressed above.

We hope our comments are helpful to the Council and we would be pleased to discuss them in further detail if necessary.

Yours truly,



Jamie Allen
Secretary General

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