The Evolving Role of the Board

By ANNABELLE YIP

The demands on directors of companies, particularly publicly listed companies, have grown exponentially. Difficulties posed by an unpredictable world and the urgent need to focus on sustainability call for a re-examination of the roles and responsibilities of the board of directors.

Directors, together with management whom they supervise, are the stewards of the company. The duties and responsibilities of directors, such as the duty to act in the company's best interest, to act honestly, to ensure the requisite level of due care, skill and diligence, and other fiduciary and statutory duties, are well-established under the Singapore Companies Act and by legal precedent.

For companies listed on the Singapore Exchange (SGX), there is an additional overlay of laws and regulations. The SGX listing rules, the Securities and Futures Act (SFA) and various regulations protect the market and safeguard the interests of a broad swathe of public investors with varying expertise, sophistication, investment horizons, interests and demands.

For example, the listing rules confer additional rights on shareholders to approve certain matters such as interested person transactions and major acquisitions and disposals that would otherwise be under the purview of the board, and impose other requirements on issuers. The SFA includes market-protective provisions such as insider trading laws and regulations governing market conduct.

Corporate governance

Listed company directors must be cognisant of all these applicable laws, rules and regulations. They also have to be mindful of corporate governance best practices and the expectations of regulators and investors, as these have reputational and other implications for companies.

Singapore's Code of Corporate Governance (Code) which sets a benchmark expectation of corporate governance best practices remains largely applicable on a comply-or-explain basis, although the Code's 13 broad Principles are now mandatory. The current Code (2018 version) is the fourth edition of the Code since it was first issued in 2001.

Since the first Code, corporate governance concepts have been instilled into company directors and management in Singapore. Some, such as the need for independent directors, have firmly taken root with almost all listed companies in compliance, while others – remuneration disclosures and gender diversity, for instance – have stubbornly remained quite elusive.

The SGX Regulator's Column released on 5 May 2022 is a timely reminder of the duties of directors under the SGX listing rules. The column provides an overview of directors' legal duties as well as their role in upholding standards of corporate governance. It sets out SGX's expectations of listed company directors in situations commonly faced by them and the importance of disclosure and transparency in Singapore's disclosure-based regime.

Sustainability and ESG

The requirement to issue a sustainability report was introduced into the SGX listing rules in 2016. In 2021, developments rapidly picked up, with the Singapore government unveiling the Singapore Green Plan 2030 – a whole-of-nation movement to advance Singapore's national agenda on sustainable development.

SGX soon followed up with new listing rules introducing, among others, the disclosure in the sustainability report of climate-related information consistent with recommendations made by the Task Force on Climate-Related Financial Disclosures, mandatory training of all directors on sustainability, and detailed disclosure requirements on board diversity.

The SGX listing rules make it clear that the board has ultimate responsibility for the issuer's sustainability reporting. In addition, the listing rules require the sustainability report to describe the roles of the board and management in the governance of sustainability issues.

Importantly, while it is often in the context of sustainability reporting that environmental, social and governance (ESG) strategy is discussed, the focus is ultimately not just on reporting and disclosure. Sustainability reporting frameworks provide a useful lens for identifying and understanding the ESG and climate-related risks that companies face. However, it is proactive management and mitigation of the risks associated with the identified material ESG factors that is critical.

Challenges today

Cyber security remains of critical importance, with companies and states falling prey to ransomware, data breaches and cyber attacks. On the flipside, companies have to keep up with rapidly developing artificial intelligence and other technologies that have the potential to enhance their competitiveness and service offerings, or risk falling behind their competitors.

The challenges for boards and management today are perhaps more extensive and complex than ever before. Risks (and opportunities on the other side of the coin) abound in many new, previously unencountered areas.

In the area of political risk, boards and board committees overseeing risk have their work cut out. While political risk may have been previously contained within a country or region, it often now is on a larger scale, cross-jurisdictional, bound up with legal and other risks (for example, sanctions), fast-developing and unpredictable.

Companies have traditionally diversified into new geographies as a means of expanding into new markets, but today, the choice of geographies is particularly fraught with uncertainty.

For instance, few would have predicted China's sudden ban on for-profit tutoring in core education and the strict regulation of the sector. Doing business in one jurisdiction could result in sanctions or reputational damage in another. Companies that decided not to buy Xinjiang cotton faced a huge backlash and a boycott of their brands in the huge Chinese consumer market (notably, ESG factors would have played a role in such a decision).

Boards of companies invested in Russia also had to make difficult choices when Russia invaded Ukraine. The financial impact of an abrupt, untidy exit had to be weighed against the severe and possibly lasting reputational damage of remaining in business in Russia. In this global business climate, it is often no longer possible to stay above the fray and remain neutral.

Actions that boards can take

For companies to effectively manage ESG and climate-related risks and tap the potential opportunities, boards and management must integrate ESG factors into corporate strategy – and prioritise the setting and meeting of ESG and climate-related targets.

To do this effectively, consideration must be given as to how ESG should be factored into management remuneration and performance targets. Paragraph 4.28 of Practice Note 7.6 of the SGX listing rules underscores this; it states that: *"An effective policy and operational response to sustainability risks and opportunities requires performance measurement and its linkage to performance incentives. … Clearly linking sustainability risks and opportunities with strategy, other organisational risks, operational indicators, performance measures and performance incentives not only enhances understanding but provides an engine for improvement, innovation and accountability."*

Given the role of directors as stewards of companies, non-executive directors need to understand the short-, medium- and long-term impact of ESG and climate on their companies. And directors must proactively work with management to manage the risks. This may mean regular sustainability training for non-executive directors, putting sustainability on the regular board agenda, and making it a key part of the terms of reference of a standalone sustainability committee or one of the company's existing board committees.

To help companies with a global presence understand what lies ahead in the markets where they have a presence and strategise their way forward, regular board retreats dedicated to board strategy can be key. However, they can help only if the retreat agenda is structured well, and there is proper follow-through.

Depending on the size and complexity of the group, consultants with geopolitical expertise could be engaged to provide the board with their views of the situation ahead, coupled with meaningful business advice and insights. Feedback from local management who can report on happenings on the ground will give the board a more in-depth understanding of the local situation. Committees overseeing risk should cast their net widely to include geopolitical and macro-economic risks.

Last but not least, board diversity in all its forms – including gender, age, culture, geographic background and industry experience – is critical. Together with a strong, empathetic chairperson to harness contributions from diverse board members and facilitate frank and constructive exchanges of views and perspectives, a diverse board can lead to better insights, creative solutions to problems, and deter groupthink.

These are some of the steps a board can take to address the difficulties posed by an increasingly unpredictable and unstable business environment. ■

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