

Ask Mr Sid

Dear Mr Sid

Re: Taking Umbrage with IDs

I am proud to be the executive chairman, CEO and majority (35%) shareholder of a successful listed healthcare company. To be candid, I can't imagine how anyone else would be better positioned to represent the best interests of the company and its shareholders, and to drive for the best possible results.

The company has a board of seven members. Four are independent because the rules require a majority of IDs. I brought in these IDs. You would think they would be grateful, but they hold themselves as champions of minority shareholders even though they hold few or no shares.

You could not imagine the grief they gave me when I recently sought to inject a highly profitable distributor of gym equipment that was reaching its growth limits. My son and I own and built this company from scratch. We are doing everyone a favour by synergising it with my healthcare company to make both even more successful.

It irritates me that the chair of our nominating committee (an old school friend)

is proposing that we separate the board chair and CEO positions. He seems to think there's a potential conflict of interest between the roles.

I take umbrage at his suggestion that I would not be able to handle any conflicts of interest. Why would my interests even conflict with those of other shareholders? We are perfectly aligned. We all want sustainable profits and dividends. I have more skin in the game than anyone else. Why would I act against the interests of the company? I went public to scale faster. Nothing's changed other than me sharing the success of my company with others.

Mr Sid, don't you agree that governance is best served by granting the most power to he who has the most at stake? How shall I tell the NC chair to back off?

Yours sincerely

Very-Effective-Chair-And-CEO

Dear Very-Effective-Chair-And-CEO

Your situation is not uncommon for many family businesses and entrepreneurial founders who went public to scale up. Your discomfort with IDs is also not uncommon, but it does reflect a lack of understanding of the purpose and role of IDs.

Before we discuss IDs, let me try to respond to some of your claims and questions.

What's changed: Other people's money

You say that nothing has changed except that you have now provided the opportunity for other people to partake in the company's success. But that is precisely what has changed: you have taken in money from other investors.

When you take other people's money, you have to be responsible and accountable to them. Yes, your skin is in the game, but so is theirs.

If you want to continue having a total say over how the company is run and governed, you should not have taken other people's money. The option is still open to you to take the company private, assuming you have enough financial resources to buy back the company.

Why interests may be misaligned: Subjectivity

You say that your interests are perfectly aligned with that of the other shareholders.

Well, not always. Not when there is a conflict of your personal interests with theirs.

Take, for example, your proposed takeover of the gym equipment distributor. I have two questions:

1. Is such a deal in the long-term best interests of the listed healthcare company?
2. Is the price of the private distributor right for your listed company?

I expect your answer would be: The deal and the price are right. But that would be your view and a subjective one.

You are conflicted because you stand on both sides of the deal. If the transaction did not occur, the distributor could not grow (as you indicated). But that is a rationale for the distributor, not the healthcare company. It is not fair for the healthcare company to help the distributor scale up unless it also benefits. If the price of acquiring the distributor is higher than it needs to be, this is unfair to the shareholders of the healthcare company. You are a shareholder of both, but you would personally gain more as you have 100 per cent of the private company and only 35 per cent of the public company.

To be fair to all, a collective view needs to be taken by those who are not conflicted and can be objective about the transaction. That excludes you.

Misalignment and conflict of interests are not confined to mergers and acquisitions.

It can affect any business decision. A major flashpoint for IDs is the remuneration paid out to directors and management, who are related to the shareholders.

Why would you act unfairly: It happens

You asked why you would act against the (other) shareholders' interests? You may not intend to, and you may think that you are not, but it can and has happened, at least with others.

Cases abound of allegations, lawsuits and regulatory queries and actions against boards and their controlling shareholders and executive chairpersons for acting improperly and breaching their fiduciary duties in conflict-of-interest situations. Companies in the news include Raffles Education, Amara, Lian Beng Group, Stamford Land and Hwa Hong.

Sometimes, the cases only come to light when IDs resign, especially en masse, publicly stating their disagreements.

Why separation of Chair & CEO: Good governance

You eschew the NC chair's suggestion to separate the role of board chair and CEO. Unfortunately for you, that is considered a best practice in corporate governance.

Provision 3.1 of the Singapore Code of Corporate Governance requires the board chair and CEO to be "separate persons", while Provision 2.2 requires the board to be a majority of IDs when the board chair is not an ID (otherwise, SGX Listing Rule 210(5)(c) only requires IDs to make a third of the board).

The rationale for the separation of roles is indicated in Provision 3.1: to ensure an

appropriate balance of power, increased accountability and greater capacity of the board for independent decision-making.

There are, of course, arguments for a combined board chair and CEO (let's call it "Chair-CEO"). Being deep in the business, the Chair-CEO would understand the business better, and decision-making is expedient. But the prevailing wisdom is that two heads with constructive debates and checks and balances are better than the over-concentration of power in one single individual.

The Chair-CEO is becoming an endangered species. Across the world, corporate governance codes discourage them, and the position is in decline. This is even so in the US, long a bastion for Chair-CEOs. According to Spencer Stuart's latest *US Board Index*, only 41 per cent of the S&P 500 companies had Chair-CEOs in 2021, compared to 59 per cent in 2011 and 71 per cent in 2005.

In Singapore, based on the latest *Singapore Directorship Report*, 19.1 per cent of listed companies had Chair-CEOs in 2021, down from 30.8 per cent in 2014 when SID first started the report series.

Purpose and role of IDs

The concept of IDs was introduced because of the practical realities of human nature and the desire for checks and balances.

The fact is that directors who are executives or appointees of major shareholders may sometimes make decisions – even if not intentionally or consciously – unduly influenced by the circumstances of their appointments or their roles in the companies.

But make no mistake about it: an ID is first and foremost a director. Every director has the fiduciary duty to act in the best interests of the company.

When it comes to shareholders' interests, every director should make decisions based on the overall interests of all shareholders – not just majority or minority. So saying that IDs exist to champion minority shareholder interests would not be quite correct.

But IDs do need to actively consider minority shareholder interests because the non-independent directors may not naturally do so. Part of the IDs' role is thus to guard against potential abuse of power by controlling shareholders and their nominees. But that does not mean that they work actively against the interests of the controlling shareholders. They work objectively for both sides, ensuring fairness because they do not have a stake in either.

The challenge of IDs is finding those that are truly independent. The rules only disqualify those that are related by blood and money to the management and controlling shareholders. But independence is a state of mind.

In that regard, you should consider yourself fortunate that you seem to have truly independent IDs who are willing to challenge your views and positions. You will have a better governed and higher-performing company with such constructive contention.

Yours sincerely



Mr Sid ■

Who is Mr Sid?



Mr Sid is a meek, mild-mannered geek who resides in the deep recesses of the reference archives of the Singapore Institute of Directors.

Burrowed among his favourite *Corporate Governance Guides for Boards in Singapore*, he relishes answering members' questions on corporate governance and directorship matters. But when the questions are too difficult, he transforms into Super SID, and flies out to his super network of boardroom *kakis* to find the answers.

Mr Sid's References (for this question)

Board Guide
Section 2.5: Board Leadership
Section 5.3: Duty to Act in the Company's Best Interests
Section 5.4: Duty to Avoid Conflicts of Interest

Nominating Committee Guide
Section 3.4: Board Composition
Section 4.4: Criteria for Independence

Boardroom Matters
Vol 1, Chapter 20: "The Search for Independence" by Lim Chin Hu
Vol 3, Chapter 4: "Will The Truly Independent Director Please Stand Up?" by Willie Cheng
Vol 3, Chapter 39: "Duties In and Consequences of Conflict of Interest Situations" by Gerard Tan
Vol 3, Chapter 42: "How Would One Know That It Is A Conflict of Interest?" by Gerard Tan
Vol 4, Chapter 28: "Preparing for an Independent Director-led Board" by Victor Yeo

Directors Bulletin
2017 Q2: "The Executive Board Chair: Boon or Bane?" by Wong Su Yen
2017 Q2: "The Independent Director: A Cut Above Or the Same as Other" by Philip Anderson
2019 Q2: "Rights and Plights of Minority Shareholders" by Victor Yeo
2021 Q2: "Trusting in the Independence of Independent Directors" by Mak Yuen Teen