THE GOVERNANCE CHALLENGE: COMPLIANCE VERSUS EXCELLENCE IN SINGAPORE

Annual Spencer Stuart Singapore Board & CEO Summit

Corporate governance and compliance are receiving renewed attention today in light of recent modifications to Singapore's Governance Code — including changes in requirements for director independence, board composition, director training and risk management. Boards in the region have been working diligently to comply with the new standards and improve their governance. Yet, even companies with the best intentions can fall into the trap of taking a check-the-box approach to governance, solely focusing on compliance. When they do, boards can miss out on the potential to elevate their performance — and the performance of their companies.

Spencer Stuart recently gathered board directors and CEOs from within Singapore and throughout Asia to discuss the new governance requirements and, more importantly in our view, the practices that help boards go beyond compliance to have a more meaningful impact on the performance of the business. **Mr. Kai Nargolwala**, lead independent director of Singapore Telecommunications (SingTel) and board member of Prudential, PSA International, Clifford Capital, Duke-NUS Graduate Medical School and Casino Regulatory Authority of Singapore; and **Mr. Jackson Tai**, board member of Bank of China, MasterCard, NYSE Euronext, Philips Electronics and Singapore Airlines, shared their firsthand insights about key issues directors in the region face and how boards can transcend compliance and pursue excellence.

SpencerStuart

Performance under pressure

Boards are pulled in an increasing number of directions today, from compliance and strategy to CEO succession and risk management. In order to balance these multiple demands, Mr. Nargolwala advises that boards empower their committees, especially the audit, risk and compensation committees, to free up time for the full board to focus on long-term strategic issues. According to Mr. Nargolwala, those topics are: selecting and developing the right executive talent (especially the CEO), strategic positioning and board performance issues, such as whether the board is receiving the right information from management.

Given the wide range of board responsibilities, it can be difficult for directors to determine where the board's reach ends. The key to determining the board's scope is having clearly defined and delineated responsibilities for the board and management. Ideally, management develops the strategy and engages the board when making a decision about a course of action and when the strategy must evolve.

"Governance can be too prescriptive and mechanical," said Mr. Tai. "The role of the board is to ask the right questions, especially about strategy. Boards can be too obsessed with past performance, but given the increasing speed, scale and reach of technology and social media, they need to be more forward-looking." Mr. Tai suggested boards think about how to anticipate disruptions as well as how to mobilize resources and establish key performance indicators to address both threats and opportunities.

Boards may assume different levels of responsibility depending upon the company's stage of evolution. Similarly, the role of the chair evolves along with the stage of the company. Mr. Nargolwala observed that early-stage companies may benefit from a hands-on chair or a board member with operating experience who can act as a mentor. As the company grows, the chair's focus should shift to building and leading the board. In Singapore, there is a demand for individuals who can serve as nonexecutive chairs. Given the time commitment demanded of the chair, he or she should be in the same location of the company, rather than live overseas.

Because the dynamic between the chairman and CEO is so important, Tai argues that the chair should have previously held a CEO or other very senior executive role. The chair also must be able to strike a delicate balance between respecting the CEO's role in running the company and having the courage and ability to rise to the occasion when the situation demands it.

To work most effectively, it is important that board members, the CEO and the chair foster their relationships outside the boardroom in order to build understanding and trust between them. These

"The role of the board is to ask the right questions, especially about strategy. Boards can be too obsessed with past performance, but given the increasing speed, scale and reach of technology and social media, they need to be more forward-looking."

Mr. Jackson Tai

An executive assessment conducted by an independent party can prove especially useful in illuminating the strengths and developmental needs of CEO succession candidates.

relationships are especially important in Singapore. "There is a saying in the United Kingdom that Americans meet to talk and the British talk to meet," said Mr. Nargolwala. "Singapore is more like the U.K. in that regard. Many topics are hard to object to in the boardroom." It is important to use judgment in determining when to discuss challenging topics outside of the boardroom, prior to a meeting.

Although it is natural to strive for consensus, board members must feel comfortable asking questions and, when necessary, raising objections. Strong relationships among the CEO and directors should enable healthy and necessary debate. One tactic the chair can adopt to encourage healthy dissent on the board is to nominate a director to take the minority opinion about a particular issue and convey its strengths. Appointing a "devil's advocate" removes the social pressure while maintaining the integrity of the discourse, said Mr. Nargolwala.

Arguably, one of the board's most critical roles is CEO succession planning. Before the current CEO and other key leaders approach retirement, boards should identify the key skills and attributes that will be necessary for the next chief executive. Especially in Asia, where demand for experienced leaders continues to exceed supply, boards should have ongoing discussions about potential candidates, regularly evaluate and create development plans for potential successors and consider a variety of succession scenarios.

One challenge to having robust discussions about CEO succession and internal successors can be that directors in Singapore can have varying degrees of exposure to management. An executive assessment conducted by an independent party can prove especially useful in illuminating the strengths and developmental needs of succession candidates so that the board has a shared understanding of the company's next generation of leadership.

Finding and keeping the right board members

The Singapore Governance Code will likely spur additional demand for new directors in an already shallow talent pool: the regulation requires that half of the board be independent if the chair is not. In Singapore, finding independent directors can be especially challenging, since many boards rely on their existing networks when looking for new members. As Mr. John Lim, chair of the Singapore Institute of Directors, said at a recent conference, "Whether we like it or not, in Singapore, appointment to boards has historically been by referrals and references." High-performing boards will strive to challenge long-held board recruitment practices in order to truly bring fresh perspectives to the boardroom.

More Singapore business leaders are recognizing

that greater board independence is a necessary cultural shift. "Board members should not be added through the referral process," said Mr. Nargolwala. "It cannot be an old boys' club. Boards hold too much responsibility to not be scientifically established and refreshed."

One barrier to finding directors who meet Singapore boards' wish lists is inadequate compensation for the time required for board service. To attract and retain qualified members, boards in the region may need to become more flexible, reducing the frequency of meetings or hosting more meetings via video-conference or telephone rather than in-person. An independent third party can provide boards with guidance about competitive compensation and bring objectivity to the selection process. At the same time, the third party does the difficult work of rejecting candidates, saving board members from performing that task and possibly jeopardizing relationships in a small community of leaders.

In addition to serving as a barrier to true board independence, the current candidate referral culture of Singapore boards also can impede the advancement of women into the boardroom. According to the *Singapore Board Diversity Report: A Focus on the Female Factor*, Singapore lags behind the global average and other developed countries in female board representation at 7.3 percent.[1] By comparison, several European countries have adopted regulation or voluntary targets to increase the percentage of women serving on corporate boards, and more may follow. Thanks to these efforts, Norway has 40 percent female board representation, Finland has 27 percent and Sweden has 26 percent. In the United States, women currently make up 17 percent of S&P 500 boards.

Although quotas regarding female representation on boards are being debated elsewhere in the world, Mr. Nargolwala does not believe a mandate would be effective in Singapore because the pool of directors is narrow and many companies do not allow senior executives, such as those from the legal and accounting functions, to sit on boards. Still, customers, shareholders and employees expect proper representation of women, and companies risk losing credibility (and potentially business and investors) if they remain behind on these efforts. Thus, he recommends that boards in Singapore take the issue of gender diversity seriously and act proactively.

As boards seek to increase their independence and diversity, they can use director recruitment to add other important expertise, including specific industry and functional knowledge. Forward-looking organizations have been employing the best practice of adding board members with experience in areas that reflect the company's strategic direction or new strategic priorities. Of course, boards may have to make tradeoffs. For example, as SingTel continues its transformation from a utility to a digital company, it has been difficult to locate directors with both board experience and content expertise in emerging technologies, Mr. Nargolwala said.

[1] Dr. Martha Dieleman and Maythil Aishwarya, "Singapore Board Diversity Report 2012: The Female Factor," Centre for Governance, Institutions and Organisations, National University of Singapore, Oct. 12, 2012. http://bschool.nus.edu/Portals/0/images/CGIO/Report/SingaporeBoardDiversityReport2012.pdf.

Some suggest alternatives to subject matter experts serving as a regular board members. As Mr. Nargolwala pointed out, one solution often seen in science and technology companies is having an advisory board composed of experts that regularly interacts with the board of directors, with one technically oriented board member serving as a bridge between the two groups.

Ongoing excellence

Just as the board is charged with evaluating potential CEO candidates, it must also turn the microscope on itself and assess its own priorities, strengths and opportunities for development. Although Singapore boards must conduct an annual self-evaluation for the sake of governance compliance, consistent and continuous reflection is extremely valuable in the pursuit of excellence.

According to Mr. Tai, many companies stop at a checklist form for board evaluations, which does little to change governance processes. These boards tend to be fearful of the outcomes of in-depth evaluations. But limiting self-evaluation with a checklist or scorecard is overly mechanistic and can result in decimal point differences. He worries that by their very quantitative nature, these scorecard evaluations and other similar mechanical processes cannot provide the relevant qualitative action items boards need to actually improve their performance. Boards can benefit from using an experienced third party to interview directors, synthesize the data and provide a summary with commentary about how to improve performance. These reports, then, can serve as a catalyst for board discussion and, ideally, will give boards the information they need to set specific goals for addressing areas in need of improvement. As lead independent director at SingTel, part of Mr. Nargolwala's role is to collect feedback from his fellow directors, combine it and deliver it to the chair.

> "Board members should not be added through the referral process. It cannot be an old boys' club. Boards hold too much responsibility to not be scientifically established and refreshed."
>
> **Mr. Kai Nargolwala**

Concluding points

The revisions to the Singapore Governance Code are meant to increase boards' independence and enhance their role in risk management. Although the new code has introduced a number of useful initiatives, no code in and of itself can ensure optimal board governance. It is ultimately up to the members of the board — in particular, the chair, CEO and committee heads — to aggressively move beyond compliance, especially in the areas of director selection and board evaluation. Diversity of thought, experience and background among directors can bring much-needed fresh perspectives to the boardroom. In order to truly maximize the board's contributions, evaluations need to accurately and thoroughly reflect performance and provide actionable items for improvement. Boards and companies that go beyond simply checking the box and that take the opportunity to truly evaluate their weaknesses and build upon their strengths stand to truly reap the benefits of strong governance.

Panelist biographies

Mr. Kai Nargolwala is the lead independent director of Singapore Telecommunications and serves on the board of Prudential PLC, PSA International, Clifford Capital, Duke-NUS Graduate Medical School and the Casino Regulatory Authority of Singapore. He was recently the nonexecutive chairman of Credit Suisse Asia Pacific following his appointment as CEO of Credit Suisse Asia Pacific.

Mr. Jackson Tai is currently a board member of Bank of China, MasterCard, NYSE Euronext, Philips Electronics and Singapore Airlines. He was previously the vice chairman and CEO of DBS Group Holdings.

ABOUT SPENCER STUART

Spencer Stuart is one of the world's leading executive search consulting firms. Privately held since 1956, Spencer Stuart applies its extensive knowledge of industries, functions and talent to advise select clients — ranging from major multinationals to emerging companies to nonprofit organizations — and address their leadership requirements. Through 54 offices in 29 countries and a broad range of practice groups, Spencer Stuart consultants focus on senior-level executive search, board director appointments, succession planning and in-depth senior executive management assessments.

Stay Connected to Spencer Stuart

@SpencerStuView

Amsterdam
Atlanta
Barcelona
Beijing
Bogota
Boston
Brussels
Budapest
Buenos Aires
Calgary
Chicago
Copenhagen
Dallas
Dubai
Frankfurt
Geneva
Hong Kong
Houston
Istanbul
Johannesburg
London
Los Angeles
Madrid
Melbourne
Mexico City
Miami
Milan
Minneapolis/St. Paul
Montreal
Mumbai
Munich
New Delhi
New York
Orange County
Paris
Philadelphia
Prague
Rome
San Francisco
Santiago
Sao Paulo
Seattle
Shanghai
Silicon Valley
Singapore
Stamford
Stockholm
Sydney
Tokyo
Toronto
Vienna
Warsaw
Washington, D.C.
Zurich