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Perception is Reality in Conflicts of Interest

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The last article explored the duty of directors in dealing with conflicts of interest, and how full disclosure and appropriate actions are necessary to discharge a director's fiduciary duties.

But conflicts of interest have an impact that can be felt beyond the legal sphere. Individual breaches often have an equally serious bearing in the court of public opinion that can leave a stain that is difficult to remove.

For example, in the 2011 case of KXD Digital Entertainment Limited, the SGX reprimanded the company and Liu Fusheng, its former chairman and CEO, for their failure to announce and seek shareholders' approval for interested person transactions and other breaches of the Listing Rules.

Damningly, it said: "Mr Liu has grossly failed to demonstrate qualities and standards expected of directors and the management of SGX-listed companies (and) SGX-listed companies are advised to consult the Exchange before they appoint Mr Liu as a director or member of management."

To be labelled unfit to be a director can sound the death knell of future directorships. The importance of carefully managing conflicts of interest and any resulting reputational risk cannot, therefore, be over-emphasised.

WHEN PERCEPTION IS GREATER THAN FACTS

Managing conflicts of interest is challenging not only from a governance perspective; the sensitive nature of the subject has a high probability of attracting adverse media publicity and stakeholder perception. As far as stakeholders and the investing public are concerned, perception can be greater than facts.

The recent saga of Singapore Post illustrates this.

In December 2015, SingPost acknowledged that it had not properly disclosed a director's interest in a 2014 acquisition due to an "administrative oversight". The ensuing reaction from market watchers that were largely played out in the media led to the appointment by SingPost of a special auditor to scrutinise the conflict of interest issues surrounding the acquisition, and the commissioning of a separate corporate governance review to address any wider governance issues within the group.

However, the appointment of the accounting firm which is SingPost's external auditor as the special auditor to review the director's conflict of interest widened the controversy. It raised questions in the media as to whether the accounting firm's two roles

are in conflict and affect its independence. To quell the concerns, SingPost appointed a law firm as joint special auditor.

With the release of the special auditors' report in June 2016, SingPost announced new policies governing directors' conflict of interests and board renewal. It also introduced a code of business conduct and ethics for its board of directors. Since the case broke, three board members including the chairman and deputy chairman have stepped down.

Yet, by many standards, SingPost had a good track record on corporate governance. Over the years, it has done better than most companies on corporate governance rankings such as the Governance and Transparency Index. These rankings show that companies can always improve on their corporate governance practices in some way or another. It was therefore unfortunate for SingPost that an administrative oversight about an undisclosed conflict has put the company under the harsh glare of the media spotlight.

BEYOND LEGAL COMPLIANCE

Such cases illustrate the difficulties facing directors and boards when dealing with conflicts of interest. Indeed, best practices require directors to go beyond their legal obligations in such situations, to the extent of removing any possible misperceptions and questions of unprofessional or unethical conduct. Some guidance can be found in the SID's Statement of Good Practice (SGP) No 5 on Conflict of Interest.

Where directors are uncertain as to whether or not they are in a position of conflict, the SGP advises them to always consult the chairman of the board or nominating committee and/or seek professional advice. Should a conflict of interest exist, the director is legally bound to disclose it to the board promptly in writing or have

it documented by the company secretary. The rules on interested person transactions under Chapter 9 of the SGX-ST Listing Rules and the disclosure requirements under Singapore Financial Reporting Standard 24 on related party transactions should always be borne in mind.

Boards involved in a conflict of interest situation must also be mindful of the repercussions of poor management of the issue. It is a weak defence to plead that directors had stuck to the form rather than the spirit of the law and rules of conflict management.

Although there is no rule of law prohibiting conflicted directors from participating in discussions on the conflicted matters, they should at least offer to recuse themselves from the meeting. They should not participate unless they are specifically invited by the board to do so, or they have the board's consent, and they believe they are able to provide relevant information without which the board might make an unsound decision.

Whether or not there is any explicit prohibition (some companies' constitution prohibits voting by conflicted directors), directors should not vote on conflict-related matters. In fact, they should offer to excuse themselves from the meeting at the time when voting takes place.

The SGP also advises directors to consider resigning from office where they have a continuing material conflict of interest or where the conflict is likely to affect the effective performance of their duties.

In summary, even if a (potential) conflict does not result in any regulatory breach, the ensuing adverse media attention and public scrutiny will not do the directors or their company any good. Developing and implementing a clear conflict of interest policy that goes beyond legal compliance is therefore a key step that all boards should take to help ensure good governance and maintain a positive public image. ■