



# The Director's Duty In Sustainable Governance

**Kala Anandarajah, Head Competition & Antitrust and Trade Practice and Lead Partner, Corporate Governance Practice, Rajah & Tann**

This article takes a quick dive into whether directors' duties have now been increased given the need for sustainable reporting. It concludes that there has been no increase in the directors' obligations, save for the need to provide a report on what they are expected to adhere to.

## How does sustainable governance fit in with corporate governance?

The term "corporate governance" is not a term of art and there is no universally agreed upon definition. One of the early definitions, often referenced today, is by Sir Adrian Cadbury who in 1999 explained the concept of corporate governance as follows:

"Corporate governance is holding the balance between economic and social goals and between individual and communal goals. The governance framework is there to encourage the efficient use of resources and equally to require accountability for the stewardship of those resources. The aim is to align as nearly as possible the interests of individuals, corporations and society. The incentive to corporations is to achieve their corporate aims and to attract investment. The incentive for states is to strengthen their economics and discourage fraud and mismanagement."

Embedded within this definition is a call for balancing profit maximisation with the greater good for society. In like view, in the words of Dave Packard, the co-founder of Hewlett Packard Company:

"I think many people assume, wrongly, that a company exists simply to make money. Whilst this is an important result of a company's existence, we have to go deeper and find the real reasons for our being. As we investigate this, we inevitably come to the conclusion that a group of people get together and exist as an institution that we call a company so that they are able to accomplish something collectively that they could not accomplish separately – they make a contribution to society, a phrase which sounds trite but is fundamental."

For traditional proponents of corporate governance, this explanation is a difficult pill to swallow as, on the face surface, it appears to undermine the very basis of why a business entity is formed. Surely making money must be for the prime purpose of profit maximisation. As observed by Milton Friedman:

"There is one and only one social responsibility of business – to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engage in open and free competition, without deception or fraud."

Yet, the call for sustainable governance is on the rise and new rules have been introduced for listed companies. Listing Rule 711A of the Singapore Exchange Listing Manual requires every listed company in Singapore to prepare an annual sustainability report, which must describe the company's sustainability practices with reference to material environmental, social and governance factors. The Code of Corporate Governance additionally provides that the board's role includes the need to consider sustainability issues at all times as part of its strategic formulation.

In essence then, the introduction of sustainable governance is not entirely new but goes back to how Sir Adrian Cadbury had defined corporate governance. Sustainable governance reminds the company to take a holistic longer-term view of the company's interests.

In this regard, whilst there has been no clear definition as to what sustainable governance means, drawing from literature, and Practice Note 7.6 of the SGX Sustainability Reporting Guide, what we do know is that sustainable governance is intended to encompass environmental, social and governance (ESG) factors. ESG is explained as encompassing materials, energy, emissions, effluents and waste, corruption, and diversity factors such as gender, skill and experience. The list of ESG factors is not closed.

## Does sustainable governance increase a director's duties?

Paragraph 3.1 of the Practice Note 7.6 of the SGX Sustainability Reporting Guide states that “the board’s close interaction with management will enable the board to satisfy itself on the way sustainability governance is structured and functioning through the various levels of management. The board has ultimate responsibility for the issuer’s sustainability reporting”. Without more, this expectation appears to require more from the directors. It is yet another review and reporting obligation that directors must now take responsibility for.

However, when one scrutinises what is required of sustainable reporting, it becomes clear that it is a function that the board has always been responsible for. The only addition is the preparation of the report that must now be included into the annual report.

In this regard, Section 157(1) of the Companies Act provides that a director shall at all times act honestly and use reasonable diligence in the discharge of the duties of his office. This requirement has been the subject of numerous court cases in various jurisdictions, including Singapore, and has summarily been interpreted as acting with due skill and care in the best interest of the company. The duty translates into the directors needing to interact closely with management to have a better understanding of the business of the company, so as to drive strategy as appropriate, to ensure compliance with all laws as business is undertaken, to better aid in enhancing the wealth of the company, and to be responsible for the long term success of the company.

In other words, the new sustainability reporting requirements do not increase the duties owed by a director; it is already encompassed in the role he performs. What is different is that the elements are now to be expressly articulated in the Listing Manual, the Practice Note and the Code of Corporate Governance.

There can be no argument that the director’s duty as such loses its objectivity. One reason for this is that a director is required to always act in the best interest of the company. Stating that a director’s duties are akin to the maintenance of a strict degree of ethics, Laskin J. in *Canadian Aero Service Ltd versus O’Malley* observed as follows:

“... Strict application [of duties] against directors ... is simply recognition of the degree of control which their positions give them in corporate operations, a control which rises above day-to-day accountability to owning shareholders and which comes under scrutiny only at annual general meeting or at special meetings. It is a necessary supplement, in the public interest, of statutory regulation and accountability which themselves are, at one and the same time, an acknowledgement of the importance of the corporation in the life of the community and of the need to compel obedience by it and by its promoters, directors and managers to norms of exemplary behaviour.”

It is also worth highlighting that “being a director is not an easy matter, and requires a responsible approach”, as was observed in the English High Court in *In the Matter of Sunrise Radio Ltd & Ors versus Dr Avtar Lit & Ors*. The court went on to note that:

“The degree of regulation can catch the most sophisticated of directors unawares. Most directors do not have the requisite level of sophistication and skill to cope unaided with the extensive statutory framework to which they are subject, or the niceties of the company’s constitution. Many become directors of companies to take advantage of limited liability, so as to exploit their entrepreneurial skills and instincts, and may not be temperamentally suited to statutory control or constitutional restraint. There is a strong public interest in encouraging entrepreneurial activity. There is equally a strong public interest in combating abuse which limited liability too often engenders.”

This case is eight years old and well articulates the point that the number of regulations is not what increases a director’s duties. Time and time again, it has been acknowledged that the principle based approach of managing directors’ duties as captured in Section 157(1) of the Companies Act, does include basic ethics, integrity and hence, a clear consideration of all factors that go towards ensuring the best interest of the company is protected. Directors need to accept that their role has always come with holistic responsibilities, which rules and guidelines are now providing guidance for. There is no creation of new obligations. •