Board charter

MCCG Intended Outcome 2.0
There is demarcation of responsibilities between the board, board committees and management.

There is clarity in the authority of the board, its committees and individual directors.

MCCG Practice 2.1
The board has a board charter which is periodically reviewed and published on the company’s website. The board charter clearly identifies—

- the respective roles and responsibilities of the board, board committees, individual directors and management; and
- issues and decisions reserved for the board.

(The application of this Practice in its entirety entails the establishment of a board charter as well as a periodic review and publication of the board charter on the company’s website.)

The internalisation and application of the content “Why” and “How” should be read in tandem with the line of sight outlined by the Intended Outcome.

Why

The case for change

Whilst the general roles and responsibilities of boards are well founded, the expectations on directors have evolved significantly owing to changes in the corporate landscape. High-profile board failures, the boom in responsible investing, and the disruptive forces of technology are placing directors under an unprecedented level of pressure from shareholders, regulators and other stakeholders.

In response to this change, directors today are expected to deal with a breadth of issues in a timely manner. A study of over 1000 global companies by McKinsey in 2015 (as shown on the following page) highlighted that directors are increasingly deepening their commitment, investing more time and going beyond the minimum prescribed to engage more deeply on aspects such as strategy, performance management and stakeholder management.

What could go wrong:
- Expectation gap between the board, management and other stakeholders regarding the board’s role.
- Selected individuals having unfettered power of decision-making.
- Directives by the board are not acted upon in a timely manner by management.
- Deliberations and decision-making are dominated by certain individuals.
- Lack of a structured approach to board proceedings, resulting in ineffective deliberation and decision-making process.
In tandem with this heightening demand for greater accountability, it is imperative for the board to clarify its responsibilities as well as that of the board committees, individual directors and management. Considering the accountabilities through the lens of each of these positions can provide the board with a holistic view of corporate governance. As the former CEO of Medtronic and a veteran of ten corporate boards, William George puts it, “one’s perspective on board governance depends on the board seat one holds”\(^1\).

To this end, the establishment of a **board charter** would go a long way in defusing potential tensions at the outset by clearly defining the roles of the respective parties as well as establishing well-understood boundaries. The board charter will serve as an authoritative policy document that sets out the board’s strategic intent, authority and terms of reference.

### Point for reflection

There is an increasing blurring of lines between the roles of the board and management. Directors today are demanded to be more vigilant in the operations and drivers of businesses including having an understanding of the technical details. Directors are also expected to have a granular understanding of the business model, be able to challenge assumptions underlying the strategies proposed and to master the complexities of risk management. Such expectations call for boards to become more involved and engaged, thus leading to the **“oversight versus micromanagement debate”**.

The blurring of lines becomes more apparent when the company is at a critical stage of development or when it goes through periods of stress, crisis or trust deficit, all of which necessitates a greater intervention amongst directors.

As the board cannot both manage and oversee, it is essential for the delineation of roles to be clearly crystallised to avoid overlaps in the points of accountability. Being the focal point of the company, the board should at all times exercise collective oversight of the board committees and management.

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1. The CEO guide to boards 2016, McKinsey Quarterly
The practice in substance

It is therefore clear that the board should formalise a board charter to serve as a primary reference and literature that guides the governance and conduct of the board.

Given that the charter is an avenue to communicate the company’s approach to governance, the document should be published on the website and made accessible to all stakeholders of the company. This would allow stakeholders to understand the practices put in place by the directors in discharging their responsibilities towards the company and its stakeholders.

Similar to Practice 2.1 of MCCG, Standard 8.2 of Bank Negara Malaysia’s Policy Document on Corporate Governance states that the board must have a board charter that sets out the mandate, responsibilities and procedures of the board and the board committees, including the matters reserved for the board’s decision.

Key considerations relating to the application of this Practice are outlined below:

What should be encapsulated within a board charter?

The following are some of the matters that should be considered when developing a board charter:

- a general outline of the board’s purpose, key values, ethos and principles;
- an overview of the board’s monitoring role;
- structure and membership;
- a formal schedule of matters reserved for the board, including the type and nature of issues, transactions and thresholds and the process for deliberation;
- appointment of board committees;
- roles and responsibilities of the board, board committees and individual directors;
- expectations on time commitment and protocols for accepting new directorships;
- director’s orientation and education programme;
- agreed upon procedures in enlisting independent professional advice at the company’s expense in furtherance of the directors’ duties (whether as a board or in their individual capacity); and
- procedures for the development, undertaking, and improvement of board processes, including the assessment of performance and continuing education and development of the board, its committees and directors.

Dos

- Having a periodic discussion between the board and management to ensure the content set out in the board charter reflects the company’s current needs.
- Ensuring the board charter is sufficiently detailed to capture the types and nature of issues that are to be dealt with by the board, board committees, individual directors and management.
- Making the delegation of authority clear and ensuring that such delegation is in line with the legal and regulatory requirement.

Don’ts

- Having a board charter which is overly broad and general, which is of little value to shareholders to understand the delineation of roles and responsibilities within the board or between the management and the board.
- Maintaining that the responsibilities of the various parties as encapsulated in the legal and regulatory requirement is the be-all and end-all.
- Utilising an existing board charter template that does not reflect the company’s needs and nuances.
- Poor implementation of the elements contained in the board charter.
Illustrative outline of board charter

Outline of board charter:

- Introduction
- Role of the board
- Board reserved powers and responsibilities
- Board membership, independence and conduct
- Role of the chairman
- Role of the company secretary
- Delegation to management
- Committees
- Meetings
- Declaration of interests
- Access to management
- Access to independent professional advice
- Induction and training
- Review of board performance and charter

Salient features of the Charter:

- **Matters reserved for the board** – identifies issues that need to be finally decided on by the Board.
- **Role profiles** – defines and clearly separates the roles of the Group Chairman and the Group Chief Executive, as well as the Board’s expectations of the chairmen of the Board Committees.
- **Delegation to management** – outlines that the Chief Executive Officer is responsible to the Board for the development and implementation of strategy, as well as the day to day management.
- **Terms of reference of board committees** – outlines the approved mandates of each Board Committee.

The Board undertakes an annual assessment of its performance including its performance against the requirements of its charter, the performance of individual Committees and the performance of individual Directors.

*Source: Telstra Ltd Board Charter October 2015 (Australia)*
What are the underlying principles to consider when demarcating the responsibilities between board, board committees and management?

In carrying out the delineation of responsibilities, the board should be guided by the following principles:

Delegate, not abdicate

As stated in Section 211(1) of Companies Act 2016, “the business and affairs of a company shall be managed by, or under the direction of the Board”.

It should be noted that whilst the board may appropriately delegate its authority to board committees or management, it should not abdicate its responsibility and should at all times exercise collective oversight of the board committees and management.

The board should not delegate matters to a committee or management to an extent that would significantly hinder or reduce the board’s ability to discharge its functions.

Supplement, not supplant

The board may engage on the field but shall not excessively intervene on the operational and implementation role of management.

The over interference with the management of the company’s processes, people and administration, in a manner which is intrusive may slow down or even inhibit business processes. Such actions of micromanagement could also create conflict and lead to demotivated management.

A case study which involves a director wrongfully imposing his will to a member of the management team for an unlawful purpose is described on the following page:

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2 Section 216(2) of Companies Act 2016 states that where the directors have delegated any power, the directors are responsible for the exercise of the power by the delegatee as if the power had been exercised by the directors themselves. Section 216(3) of Companies Act 2016 states that the directors are not responsible under subsection (2) if -- (a) the directors believed on reasonable grounds at all times that the delegatee would exercise the power in conformity with the duties imposed on the directors under this Act and the constitution of the company, if any; and (b) the directors believed on reasonable grounds, in good faith and after making a proper inquiry, if the circumstances indicated the need for the inquiry, that the delegatee was reliable and competent in relation to the power delegated.
**Case study: MEMS Technology Berhad (Malaysia)**

**Background:**
- A non-independent non-executive director and the chief financial officer of MEMS Technology Berhad (“MEMS”) were charged in April 2009 under Section 122B(bb) of the Securities Industry Act 1983 (“SIA”) for authorising the furnishing of misleading information to the Exchange.

**Facts:**
- MEMS had reported its revenue to be approximately RM73.4 million. Its profit after tax was reported to be RM21.5 million for the twelve month period ended 31 July 2007.
- Subsequent investigations by authorities uncovered that the substantial shareholder and non-executive director of MEMS had directed the chief financial officer of the company to generate falsified documents to support fictitious orders. This was carried out through the records of a wholly owned subsidiary of MEMS, namely, SenzPak (M) Sdn Bhd.
- Evidence from the investigation also revealed that MEMS’ revenue was overstated by RM30.2 million due to the fictitious registered sales transactions for the twelve month period ended 31 July 2007.
- Both individuals pleaded guilty to the charges on February 2010. The court imposed a prison sentence of six months in addition to fines of RM300,000 each.
- MEMS was directed to rectify and reissue its accounts for the year ended 31 July 2007 and 2008. MEMS was also required to restate and re-announce its financial results for the six-month period ended 31 January 2009.

**Lessons Drawn:**
- There should be clearly defined responsibilities between the board and management with no one individual having unfettered powers to wrongfully impose his or her will on the affairs of the company. Adequate checks and balances should be put in place to safeguard against the potential of override of controls or other inappropriate influence over the governance processes and procedures.

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3. Enforcement 2017, Securities Commission Malaysia
What are the key steps involved in developing and reviewing a board charter?

The process involved in the development and review of board charter is depicted below:

The board should review its board charter periodically or as changes arise (e.g. restructuring and strategic initiatives) to ensure that the allocation of responsibilities reflects the dynamic nature of the relationship necessary for the company to adapt to changing circumstances.
Regional/international perspectives

As in the case of Malaysia, many jurisdictions including United Kingdom, Singapore and Australia have called for clear demarcation of roles and responsibilities between board and management.

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<th>Country</th>
<th>Provision(s)</th>
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<td>Singapore</td>
<td>Every company should prepare a document with guidelines setting forth: (a) the matters reserved for the Board’s decisions; and (b) clear directions to Management on matters that must be approved by the Board. The type of material transactions that require board approval under such guidelines should be disclosed in the company’s Annual Report. <em>(Guideline 1.5)</em></td>
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<td>Australia</td>
<td>A listed entity should disclose: (a) the respective roles and responsibilities of its board and management; and (b) those matters expressly reserved to the board and those delegated to management. <em>(Recommendation 1.1)</em></td>
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<td>United Kingdom</td>
<td>The board should meet sufficiently regularly to discharge its duties effectively. There should be a formal schedule of matters specifically reserved for its decision. The annual report should include a statement of how the board operates, including a high level statement of which types of decisions are to be taken by the board and which are to be delegated to management <em>(Provision A.1.1).</em></td>
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