GOVERNANCE EVALUATION FOR MID AND SMALL CAPS (GEMS)

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INTRODUCTION

The Governance Evaluation for Mid and Small Caps (GEMS) addresses the limitations of existing corporate governance indices in several respects. First, it evaluates corporate governance practices over three years rather than on an annual basis. This recognizes that corporate governance practices must be sustained, and their impact may not be immediate. Second, it focuses on observable, quantifiable and verifiable metrics that reflect actual corporate behaviour, rather than mere disclosure of policies, practices or intent to adhere to corporate governance best practices. This addresses concerns that disclosures often reflect form rather than substance and may not reflect what is actually practiced by the company. Third, unlike existing corporate governance indices, GEMS is developed specifically with mid and small cap companies in mind. It focuses on factors of importance to such companies, such as stability of ownership and succession risk, instead of a plethora of corporate governance practices that may not necessarily pass the cost-benefit test for such companies to implement. Fourth, it recognizes the importance of regulatory risk on the protection of minority shareholders, and therefore uses indicators that differentiate companies on such risk.

GEMS covers companies with market capitalization of no more than S$500 million which are listed on the Main Board or Catalist of the Singapore Exchange (SGX). This currently makes up approximately 82% of listed companies.

Companies are assessed on the following 6 broad categories with the following specified weigthings for each category:

1. **Ownership (15%)**
2. **Board and Management (30%)**
3. **Remuneration and Interested Person Transaction Risks (15%)**
4. **Quality of Financial Reporting and Internal Control (15%)**
5. **Shareholder Rights and Communications (15%)**
6. **Regulatory Risk (10%)**

GEMS also includes ‘bonus’ and ‘penalty’ items which are not captured by the main index.

OWNERSHIP

No.	Item	Guiding principle	Basis of assessment	Points
Ownership Stability and Monitoring by Unrelated Substantial Shareholders				
1.1	The largest substantial shareholder* has been a substantial shareholder of the company for at least 3 years and has not sold off shares amounting to 20% or more of his stake over the last 3 years.	The largest shareholder has been a relatively long-term investor in the company and has not been divesting his shareholding.	3 years is the average duration to be considered as a relatively long-term shareholder. (Bohren et al., 2008) The largest shareholder cannot be a nominee or securities company. A reduction in the shareholding of the largest shareholder due to new shares being offered will not be considered a divestment.	5
1.2	None of the directors, CEO or substantial shareholders buys **and** sells shares more than 4 times within a 12 month period over the 3 years.	Insiders are not dealing in shares excessively based on short-term considerations.	Transfer of shares from major shareholders to their associates is permitted. Allotment of shares is not considered a buy.	5
1.3	There are one or more unrelated substantial shareholders*.	There is check and balance by other shareholder(s).	Detailed data provided by Handshakes will be used to determine if shareholders are 'unrelated'.	5

*Note: If the company does not have a substantial shareholder at the beginning of the 3 years, the main index would be based on 90 points and re-grossed to 100 points.

BOARD AND MANAGEMENT

No.	Item	Guiding principle	Basis of assessment	Points
Board Quality and Independence				
2.1	At least one of the independent directors has industry experience.	Some in-depth knowledge of the industry is important for independent directors to provide effective oversight and guidance.	Industry experience means educational background or work experience in the major area of the company's business operations. Merely having been an independent or non-executive director of a company in the same industry is not sufficient.	3
2.2	No more than one independent director has a tenure of more than 9 years over the 3 years of assessment.	There should be renewal of independent directors to ensure fresh perspectives and to reduce familiarity risk.	To recognise that SMEs may need to retain an exceptional independent director beyond 9 years, companies will be deemed to have satisfied the criterion if they only have 1 independent director serving beyond 9 years. However, no independent director should serve beyond 12 years.	3
2.3	No more than one independent director has resigned or retired without seeking re-election after serving 3 years or less, over the 3 years of assessment.	There should not be frequent changes of the independent directors.		3
2.4	No more than one of the directors is a busy director over the 3 years of assessment.	Directors need to be able to commit adequate time to discharge their responsibilities and	"Busy director" is based on SIAS definition: Director holding full time position limited to 4 listed company directorships. "Professional	3

		should therefore not hold too many directorships.	director" is limited to 6 listed company directorships.	
2.5	Independent directors do not have relationships with the company, its directors, key officers and substantial shareholders except for the board seat.	Independent directors should not have or appear to have relationships that are likely to affect their objective and independent judgement on company affairs.	Key officers here refer to any other director, the CEO, COO and CFO. Detailed data provided by Handshakes will be used to determine the existence of relationships. Some relationships that will result in points not being awarded include: i. 2 independent directors of the company sit together on more than 2 boards ii. 2 independent directors of the company are associated with each other in another listed company, through 1 or both of them being an executive director or senior management of the second company (and vice versa) iii. 3 independent directors of the company sit together on 1 or more other listed board(s)	3
2.6	Director(s) of the company have not resigned without valid reasons over the 3 years of assessment.		Valid reasons include directors who concurrently retire from other boards, directors who do not take on more director positions within 3 months after resignation, and directors at the end of their term.	3

Quality and Stability of Management				
3.1	The CEO has at least 10 years of experience in the industry or in a related industry.	Management should be led by a person with sufficient experience in the industry or related industry.		4
3.2	There have been no more than 2 changes for each key officer position within the 3 years of assessment.	Frequent changes to key officers destabilises the management team and indicates issues with recruitment and retention of key talent or governance.		3
Succession Risk				
4.1	At least one of the key officers other than the executive chairman or Chairman-and-CEO has been with the company for more than 5 years.	The company should have an experienced successor who is able to succeed the Chairman and/or CEO.	When company has an Executive Chairman, key officers here refer to the CEO/MD/General Manager, COO, CFO, and any other executive director. In all other cases, key officers exclude the CEO/MD/General Manager.	5

REMUNERATION AND INTERESTED PERSON TRANSACTION RISKS

No.	Item	Guiding principle	Basis of assessment	Points
Key Management Personnel Remuneration				
5.1	Key management personnel remuneration i. Decreased or remained constant and both ROE and TSR increased; or ii. Increased and both ROE and TSR increased; or iii. Decreased or remained constant and either ROE or TSR increased; or iv. Increased and either ROE or TSR increased over the 3 years of assessment.	Key management personnel remuneration is not excessive.	Definition of “key management personnel remuneration” is based on FRS24: short-term employee benefits. Constant refers to a change of ±5% for key management personnel remuneration.	i. 3 ii. 3 iii. 2 iv. 1
5.2	Executive director and key management personnel are paid both fixed and variable remuneration, where i. Not more than 1 executive director or key management personnel is paid less than 20% of variable remuneration each ii. Not more than 2 executive directors or key management personnel is paid less than 20% of variable remuneration each year iii. Not more than 3 executive directors or key management personnel is paid less than 20% of variable remuneration each year over the 3 years of assessment.	A significant and appropriate proportion of executive directors’ and key management personnel's remuneration should be structured so as to link rewards to corporate and individual performance.	The ratio of fixed and variable remuneration is disclosed on a name basis. Variable remuneration component refers to performance bonus and does not include fixed bonus payments.	i. 3 ii. 2 iii. 1

Non-executive Director Fees				
6.1	Directors' fees are constant or declined over the 3 years of assessment; or Increased if any two of the following increased over the 3 years of assessment i. Number of board and board committee meetings ii. Number of independent directors iii. Total shareholder return	Non-executive director fees are not excessive.	Constant refers to a change of $\pm$5% for directors' fees.	3
Interested Party Transactions				
7.1	The company does not engage in recurring transactions with its directors, CEO, substantial shareholders and their associates.	The company should minimize the risk of any potential conflict of interest arising from interested party transactions (IPT).	IPTs include purchase of goods or fixed assets, rental of assets, rental of office space, etc. Recurring means 2 or more IPT transactions within the 3 years of assessment.	3
7.2	The company does not engage in significant transactions with its directors, CEO, substantial shareholders and their associates.	The company should minimize the risk of any potential conflict of interest arising from interested party transactions (IPT).	Significant means a cumulative 3 year average of 1% or more of net total assets (NTA) or 3% or more of revenue.	3

QUALITY OF FINANCIAL REPORTING AND INTERNAL CONTROL

No.	Item	Guiding principle	Basis of assessment	Points
External Auditor Changes				
8.1	The company has not changed its auditor in all 3 years of assessment; or The company has changed its auditor once within the 3 years of assessment and has given appropriate reasons for the change.	Unexplained change in the auditor is a red flag for potential financial reporting risk.	Appropriate reasons include when the company switches to a higher tier auditor. Appropriate reasons may also include switching from a higher tier auditor to a mid-tier auditor provided reasons are given and the company has received an unqualified audit opinion for all 3 years of assessment.	3
External Auditor Independence and Quality				
9.1	The auditor is a certified public accountant in Singapore.	The auditor should meet Singapore's regulatory standards for public accountants.		2
9.2	The auditor is a i. Big Four audit firm; or ii. Mid-tier audit firm	The company should ensure that its auditor is a reputable firm.	Big Four audit firms include: PricewaterhouseCoopers LLP, Deloitte & Touche LLP, Ernst & Young LLP, KPMG LLP Mid-Tier audit firms include: RSM Chio Lim LLP, Foo Kon Tan Grant Thornton LLP, BDO LLP, Baker Tilly TFW LLP, Moore Stephens LLP, RT LLP, Nexia TS Pte Ltd, Mazars LLP	2

9.3	The auditor i. Does not receive non-audit fees totalling more than 25% of audit fees on a recurring basis; or ii. Received non-audit fees totalling more than 25% of audit fees but on a one-off basis	The company should minimise the use of the external auditors for non-audit services in order to maintain auditor independence.	Audit fees paid to member firms are included in fees paid to auditor.	i. 2 ii. 1
External Audit Opinion				
10.1	The company has an unqualified audit opinion for all 3 years of assessment.	The auditor has endorsed the quality of the company's financial reporting.	Companies that attain an unqualified audit opinion but with an emphasis of matter do not get any points.	4
Internal Audit				
11.1	The company has an in-house internal audit (IA) function; or The internal audit function is outsourced to a Big Four or mid-tier accounting firm.	There is adequate assurance over internal control and risk management provided by a competent IA.	The head of IA must meet IIA standards. Identity of the firm, if IA is outsourced, must be disclosed.	2

SHAREHOLDER RIGHTS AND COMMUNICATIONS

No.	Item	Guiding principle	Basis of assessment	Points
Dividend Policy				
12.1	The company i. Increased or maintained dividends; or ii. Paid dividends with decreases; or iii. Paid dividends for 2 years; or iv. Paid dividends for 1 year in all 3 years of assessment.	The company returns excess profits to shareholders or retains them to fund expansion plans.	"Maintained" means total dividend declared is the same for all 3 years of assessment. Companies with both increases and decreases within 3 years, will get 4 points. The points here are indicative only. Companies which did not increase or maintain dividends over the 3 years (i.e. did not get the full 6 points) may be given up to the maximum of 6 total points based on whether they have issued a formal dividend policy and have paid dividends in accordance with the formal dividend policy.	i. 6 ii. 4 iii. 3 iv. 2
Minutes of AGM				
13.1	The company provides shareholders with minutes/notes covering the substantive points discussed in the annual general meeting.		Companies which provide recordings of the full meeting will be given the 3 points	3
Shareholder Communications				
14.1	The company has i. a corporate website in English and ii. an investor relations section on its website	The company ensures fair and effective communication with all shareholders and potential investors.		2
14.2	The company provides investor relations contact information on its		Investor relations contact include an investor relations	1

	website or annual report.		email address and/or a telephone number.	
14.3	The company is responsive to emails or calls requesting information.	The company ensures fair and effective communication with all shareholders and potential investors.		3

REGULATORY RISK

No.	Item	Guiding principle	Basis of assessment	Points
Country of Incorporation				
15.1	The company is incorporated in the country of operation or the country of listing.	The company should be subjected to core legislative requirements in the country of its operations or listing.	The country of operation is based on where senior management is located.	5
Rule of Law				
16.1	Based on World Bank's Worldwide Governance Indicators, the company operates within the top 25% of countries with strongest rule of law.	Companies operating in countries with strong rule of law have better safeguards for investors.	According to the Worldwide Governance Indicators (WGI) Project. Percentile is based on WGI's P-rank for the country of operations. Top 25% means P-rank 75 and above.	5

BONUS

No.	Item	Guiding principle	Basis of assessment	Points
Board independence				
1B	The board is at least half independent when the Chairman is not independent. The board is at least a third independent when the Chairman is independent.	Where the Chairman is not independent, the Code recommends at least half of the board to be independent. Where the Chairman is independent, the Code recommends at least a third of the board to be independent.		+3
Disclosure of Key Management Personnel Remuneration				
2B	The company fully discloses the remuneration and names of the top 5 key officers.	To encourage companies to adopt the best practice in disclosures on remuneration.		+3
Disclosure of Non-executive Director Remuneration				
3B	There is full disclosure, i.e. not in bands, with breakdown of the remuneration of each individual non-executive director.	To encourage companies to adopt the best practice in disclosures on remuneration.		+2
Disclosure of Tenure of External Auditor				
4B	The total tenure of the auditor is disclosed.	To encourage companies to be transparent about relationships with its external auditors.	This refers to tenure since the date of first appointmet	+2
Disclosure of Resources in Internal Audit Function				
5B	The company: i. Discloses the number of persons in the in-house internal audit function; or ii. Discloses the amount it spends on internal audit if it is outsourced.	To allow stakeholders to assess if the IA function is adequately resourced.		+2

Shareholder Communication			
6B	The date of the AGM is not in the last week of April or the 4 month period from the end of the financial year, for all 3 years of assessment.	Companies that chose not to hold their AGMs in the peak season for AGMs improve the ability of shareholders to participate in the AGM.	+2
Board Gender Diversity			
7B	There is at least one independent director of each gender on the board.	To recognise the importance of diversity for board effectiveness.	+2
Share Issue Policy			
8B	The company limits the percentage of shares to be offered other than on a pro-rata basis under a general mandate in all 3 years of assessment to i. Less than 10%; or ii. Between 10% to 15%; or iii. No general mandate is given.	Issue of shares on a non-pro rata basis results in dilution of non-participating shareholders.	i. +4 ii.+2 iii.+4

PENALTY

No.	Item	Guiding principle	Basis of assessment	Points
Board Quality and Management				
1P	The board size is smaller than 6 or greater than 9.	According to the Code, "the Board should examine its size and, with a view to determining the impact of the number upon effectiveness, decide on what it considers an appropriate size for the Board, which facilitates effective decision-making". SMEs should operate with relatively lean boards, but the number of directors should be sufficient to ensure adequate mix of competencies and diversity of viewpoints especially from non-executive and independent directors.		-2
2P	There are 50% or more executive directors on the board.	Although the Code does not specify an appropriate proportion of executive directors, a board which has too many executive directors will face a serious conflict in overseeing management.		-3
3P	The chairperson of any board committees is not an independent director.	This will not be in line with guideline 4.1, 7.1, and 12.1 of the MAS Code of Corporate Governance 2012.	The board committees include the audit committee, remuneration committee and nominating committee.	-2

4P	The audit committee and remuneration committee do not consist of all non-executive and/or independent directors.	The Code recommends that the audit and remuneration committees should only include non-executive directors.		-2
5P	The board is less than one-third independent	The Code recommends that there should be at least one-third of independent directors.		-2
Disproportionate Control of Voting Rights				
6P	The largest shareholder has control exceeding beneficial ownership, e.g. through the use of a pyramid structure or cross-shareholdings.	Control rights exceeding cash flow rights increases risk of large shareholders making decisions which are harmful to the interests of other shareholders (Cao et al., 2010).	Pyramidal structure means control of constituent firms by a chain of ownership relations.	-5
Poor Tone at the Top				
7P	A disqualified director joins board within 5 years of the end of disqualification.	Disqualified directors rejoining boards soon after disqualification period indicates that the board has not sufficiently considered the importance of tone at the top and appoint other suitably qualified directors who have not faced regulatory actions.		-5
8P	Director(s) and/or key officers of the company have been sanctioned (e.g., reprimanded or convicted) during the past 5 years.	Directors and/or key officers who have been sanctioned indicate a weak tone at the top and would also raise issues about the governance of the company.		-5 to -10 for each director or key officer
Poor Disclosure on Board Meetings and Attendance				
9P	The number of meetings of the board and board committees held is not disclosed.	Companies that do not disclose the number of board meetings are not being accountable to shareholders and this is a deviation from a key disclosure guideline in the Code.		-2

10P	The attendance of every board member at the board meetings is not disclosed.	Companies that do not disclose the attendance of directors at board meetings are not being accountable to shareholders and this is a deviation from a key disclosure guideline in the Code.		-2
Poor Disclosure of Remuneration of Key Management Personnel				
11P	The company discloses remuneration of any of its key management personnel with an unlimited top band.	Companies that disclose remuneration with an unlimited top band have violated the disclosure guideline 9.3 of the Code.		-2
Use of Options for Independent Directors				
12P	Share options were issued to independent directors within the past 3 years.	The use of share options may impair the independence of independent directors.		-3
Non-Disclosure of Share Pledges				
13P	Directors, key officers or major shareholders and their associates did not disclose their pledged shares.	Any significant pledging of company shares may lead to sudden change of control or large sale of shares in the market.	Companies will be penalised if the non-disclosure becomes known or they fail to deny when questioned	-3
Modified External Audit Opinion and Restatements				
14P	External auditor issues a i. Adverse; or ii. Disclaimer of; or iii. Qualified opinion.	A qualified, adverse or disclaimer of opinion is a major red flag about the quality of the company's financial reporting or about its solvency.	Companies with an adverse opinion or disclaimer of opinion will get a higher penalty than those with a qualified opinion.	i. -10 ii. -10 iii. -5
15P	The company restated financial statements of i. 2 to 3 years; or ii. 1 year over the 3 years of assessment.	Restatements of financial statements raises concerns about the quality of the company's financial reporting.	Does not include restatements that are purely reclassifications (unless material impact on assessment of operating	i. -5 ii. -3

			performance or financial position)	
Unusual Trading and Queries				
16P	The company has been asked by SGX to suspend trading activity, or only suspended trading after repeated queries by SGX i. For all 3 years of assessment ii. For 2 years of assessment iii. For 1 year of assessment	Being issued such requests from regulators is an internal control red flag and indicates increased governance risk of the company.		i. -10 ii. -5 iii. -3
17P	The company makes a major announcement within 2 months following a "nil" response to a query regarding trading activity by SGX.	Such announcements potentially indicate insider trading has occurred at the time of the query.	Major announcements include more than 10% change in revenue, net total assets, acquisitions, disposals etc.	-3
Regulatory Actions by SGX and/or Other Authorities				
18P	The company faced regulatory actions by SGX and/or other authorities or breached listing rules in the 3 years of assessment.	Facing action by regulatory authorities is a signal of severe mismanagement of the company.	Penalty to be determined by advisory panel	-3 to -10
Poor Shareholder Communications				
19P	Annual results are not released within 60 days after the fiscal year-end or interim results are not released within 45 days of end of interim period, or the company has a late AGM.	Failure to release annual results within 60 days/45 days after the fiscal year end/interim period is a violation of SGX listing rule 705(1).		-5
20P	The AGM is held outside of Singapore without valid reason and does not provide a webcast/ videoconference for Singapore-based	Failure to hold the AGM in Singapore is a violation of SGX listing rule 730A(1).	Valid reasons refer to when company is incorporated in a country that has relevant laws and regulations that	-3

	shareholders.	prohibit the company from holding its AGM in Singapore. Companies holding AGMs outside Singapore with valid reasons must have alternative modes of engagement as required under revised SGX rules