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SIAS unveils new governance ratings system for SMEs

The research will enable investors to make informed decisions on listed firms

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Evaluating SMEs

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THE Securities Investors Association (SIAS) - together with the Singapore Association of The Institute of Chartered Secretaries (SAICSA) and data analytics firm Handshakes - on Wednesday launched GEMS, a new corporate governance ratings system for small and medium enterprises (SMEs) listed on the Singapore Exchange (SGX), which is believed to be the first of its kind anywhere.

"This is an important milestone for the local market and an important initiative for SIAS," said SIAS president and chief executive David Gerald at a press conference on Wednesday to launch GEMS. "Many retail investors are invested in medium and small caps, which represent 80 per cent of the companies listed on SGX. With this research, investors will be better able to make informed decisions about companies they invest in and also identify well-run companies."

Governance Evaluation for Mid and Small Caps, or GEMS for short, was developed with input from governance expert Mak Yuen Teen, an associate professor from NUS Business School, and targets companies with market capitalisation below S$500 million.

"Having been involved in developing a number of corporate governance ratings and scorecards, I feel that they generally rely too much on disclosures by companies and do not sufficiently differentiate between what is important for SMEs compared to larger companies," said Prof Mak.

As a result, GEMS uses data for three years instead of the more usual one year and looks at actual behaviour and actions rather than just disclosures.

"Under the ownership section for example, we'll look at whether major or substantial shareholders have over the past three years sold off more than 20 per cent of their stake, and whether major shareholders and key officers engage in frequent trading of their shares," said Prof Mak.

"Under Board and Management, we will look at the tenure of independent directors (IDs), whether at least one has industry experience and whether there are any relationships between IDs and key officers."

Points are assigned for each category; for example, under "Quality of Financial Reporting and Internal Control", companies will be assigned the maximum three points if they have not changed their external auditors over the three years, or if they have changed auditors once but have given appropriate reasons for the change.

Other categories are "Remuneration and Interested Person Transaction Risks", "Shareholder Rights and Communications" and "Regulatory Risk". Bonus points can be given for various practices, eg, three points if there is full disclosure of the pay of the top five key officers, two points if there is disclosure of resources devoted to any internal audit function, and two points if there is at least one independent director of each gender.

However, penalty points are also possible - eg, minus five points if there is disproportionate control of voting rights, -5 points if the company has been asked by SGX to suspend trading or has suspended trading only after repeated queries for all three years, and -3 points if it makes a major announcement within two months following a "nil" response to an SGX query.

There are also penalties if annual results are not released within 60 days after year-end or interim results are not released after 45 days - which would be a breach of SGX's listing rule 705 (1) - or if the annual general meeting is held late.

"Past experience shows that corporate governance failures occur mainly amongst SMEs," said Mr Gerald. "With this research and rating, GEMs will no doubt be of tremendous value to all investors. SIAS will be using it as an initial screen this year for our annual corporate governance awards."