Corporate Governance and Small Islands

Dr Chris Pierce explores the reasons why small islands have different corporate governance practices from the rest of the world.- May 2018

“One size does not fit all” is a familiar mantra for corporate governance practitioners so it should come as no surprise to hear that small islands are increasingly expressing the opinion that their governance practices are different to other countries in the World. This article by Dr Pierce examines the corporate governance challenges and practices that make small islands different.

Who are the small islands?

The United Nations have identified forty small island developing states: Antigua and Barbuda, Bahamas, Barbados, Belize, Cabo Verde, Comoros, Cook Islands, Cuba, Dominican Republic, Fiji, Grenada, Guinea-Bissau, Guyana, Haiti, Jamaica, Kiribati, Maldives, Marshall Islands, Mauritius, Micronesia, Nauru, Niue, Palau, Papua New Guinea, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Samoa, Sao Tome and Principe, Seychelles, Singapore, Solomon Islands, Suriname, Timor-Leste, Tonga, Trinidad and Tobago, Tuvalu and Vanuatu.

The distinctive challenges impacting upon corporate governance

Resource issues

The total population for all of the forty small island developing states is around 60 million people which accounts for just under one per cent of the total world population. Their small human resource base, and domestic market has had a significant impact upon their inability to benefit from economies of scale.

Trade issues

Many of the islands have a heavy dependence on a single commodity (e.g sugar cane) or a single service (e.g. tourism) and concentrate on a few external and often remote markets. Their high costs for energy, infrastructure, transportation adds to a lack of competitiveness and their economies are significantly impacted by fluctuations of the world trade cycle.

The “Brain drain” and talent shortages

In many cases, people are emigrating due to natural disasters or in search of economic or educational opportunities elsewhere. Many of these emigrants have the potential to contribute to the development of their home country but feel compelled instead to seek opportunities abroad and as a result many islands are suffering from widespread talent shortages.

Fragile environments and a vulnerability to natural disasters

Many of the islands are located in regions that have fragile environments that can be highly affected by natural disasters. There were 491 natural disasters that affected small islands between 1990 and 2013. In 2012, hurricane “*Sandy*” damaged more than 100,000 homes in Cuba at a cost of over US $2 billion also causing significant damage in Haiti, Jamaica and the Bahamas. Many climatologists suggest that these natural disasters will intensify over time as a result of climate change.

A high level of public sector activity

These islands tend to have very large and influential public sectors. The private sector at times may feel that they are not operating on a level playing field since the public sector maybe pursuing uncompetitive practices based upon their monopoly status. In order to deal with this challenge, many governments are recognising the need to develop governance guidelines and codes for the public sector. For example in Jamaica, the corporate governance framework for public bodies was revised in 2012, a competency profile instrument for the boards of public bodies was published this year and a Code of Conduct is currently being finalised.

Many islands, particularly those in the Caribbean region, have very high debt to GDP ratios (in many cases well in excess of 100 per cent) with high public debt levels being a persistent problem for a long period of time. For others, rapid debt accumulation has been a relatively recent phenomenon and poses serious problems for economic development.

Development funding

Official development assistance is funding that many islands rely on. The forty small islands each receive an average of around USD$ 160 million in official development assistance. However, there are large variations in aid allocation, for example, there was a large influx of funds to the Caribbean at the time of the 2010 earthquake in Haiti. Access to capital is often limited to bank loan finance since very few islands have their own national stock exchange.

Climate change

Collectively islands are responsible for less than one per cent of the world's greenhouse gas emissions and so the problem of climate change is not of their own making. However, many are very vulnerable to climate change and some are already experiencing: an increased frequency and intensity of storms and flooding; persistent droughts and water scarcity; rises in sea-level; coastal erosion and ocean acidification. Islands such as those in the Maldives with many low-lying atolls, are already losing significant amounts of territory due to the rising seas. Also because the coastal areas are often the most densely populated, the loss of land is having a significant impact on island society and culture.

What corporate governance initiatives are currently taking place?

The development of corporate governance codes

In the last five years many islands have developed corporate governance codes. Examples include: Mauritius (2016), Maldives (2014), Trinidad and Tobago (2013), Singapore (2013) and Guyana (2011). Since the global financial crisis, governance guidelines for banks have also been developed in many islands such as the Bahamas (2013), Barbados (2013) and Mauritius (2012) as a result of having a high national dependency upon the financial services sector, money laundering concerns and the risk of being labelled as an unethical tax haven. Many of these codes have learnt lessons from the OECD countries who have well-established codes and so these new codes have leapfrogged to the forefront of governance innovation. Examples include the Mauritian Code of Corporate Governance that contains guidelines for different sectors, scorecards, and international benchmarked data.

Focus on Sustainability and Integrated Reporting

Due to climate change there has been a need for companies to increasing their focus upon sustainability issues and report in their annual reports and on their websites on sustainability matters. Many of the islands have companies that are at the forefront of disclosure and transparency within an integrated reporting framework.

An increased focus on risk management

As a result of the vulnerabilities that the islands face boards and senior management are increasingly focusing upon developing and maintaining effective risk management, disaster planning and business continuity processes. In particular COSO and COBIT 5 frameworks are being implemented to improve governance practices.

Director selection and appointment

Due to talent shortages boards are increasingly finding it necessary to improve their methods of attracting new and talented directors. Recruitment and remuneration consultants are being established to assist board committees in their work and the Institute of Directors are also assisting boards in this area e.g. the Singapore Institute of Directors runs a Board Appointment Service to assist boards and nominating committees widen their search for competent and suitable candidates when looking for independent directors.

The growth of Corporate Governance Associations and Director Institutes

Corporate Governance and Director Institutes play a major role in providing governance advocacy and director training and this can have a major impact upon the acceptance of ever increasing corporate governance standards. Some of the Associations and Institutes have initiated awards to encourage the development of good governance practices e.g. the Singapore Institute of Directors regularly runs a "CEO of the Year" and "A Best Managed Board" award.

Some of the fastest growing Institute of Directors are currently located in small islands e.g. the Mauritius Institute of Directors has been in operation for only 6 years but now has over one thousand members. In addition, the level of sophistication of some of the director training programmes is very high and is equivalent to any of the programmes that are run by any Institute of Directors in the OECD countries e.g. the Caribbean Corporate Governance Institute based in Trinidad and Tobago launched its programme of training across the English speaking islands of the Caribbean in 2014 that includes a Certificate in Corporate Governance (7 days of training), a Diploma in Corporate Governance and a Chartered Director status.

Future focus

Islands are going to need to maintain their focus upon developing governance standards and this is likely to involve:

Structure of the board

The criteria for independent non-executive directors will need to be developed further and enforced by regulators in order to deal with the high potential for conflicts of interest and related party transactions that exist amongst islands**.**

Strategy

Effective business planning by executive management will continue to be regarded as essential for a company to survive. When boards ratify their company's strategies they will need to focus upon differentiating their services and products rather than competing directly on price.

Technology

There are considerable opportunities for islands to benefit from the enabling impacts of using new technology e.g. the usage of teleconferencing for board and senior management meetings.

Public sector / private sector mix

Policy makers will need to focus upon the appropriate levels of public sector activity and public sector debt. In many cases, monopoly abuse, public sector bribery and corruption and a lack of competitiveness within the economy needs to be addressed. Further developments in public sector governance guidelines and codes should be anticipated.

Dr Chris Pierce is CEO of Global Governance Services Ltd. based in London. He can be contacted at: chrispierce @ggs.uk.com and his company website is at www.ggs.uk.com