

ORGANISATION

Corporate governance in overseas jurisdictions

Although principles comparable to *fiduciary duties* for directors have reasonable global application in most jurisdictions, the laws and legal systems of foreign countries may differ markedly from those in Australia.

Directors of corporations operating in foreign countries should seek to ensure that they have a sound understanding of the legal systems in those countries and that the organisation has in place appropriate governance and management systems and processes to meet those legal requirements.

Of note, the duty for a director to act in the best interests of the corporation may vary in some countries to include a more extensive list of beneficiaries of the director's duties.

Directors of foreign subsidiary companies, and directors of holding companies with subsidiary operations in other countries, should carefully consider and appropriately structure the governance framework and practices under which the corporate group operates.

Special care needs to be taken with respect to corrupt practices and bribery risks in a number of foreign countries especially given the severity of penalties and the reputational risks that may be involved for both the corporation and its directors, as well as the restrictive nature and reach of the bribery and corruption laws of countries such as UK and USA.

Directors who operate in an international context continue to have a governance and directorial oversight, not a detailed hands-on management role. Directors of companies operating overseas, or directors sitting on the boards of overseas subsidiaries, are not expected to have specific knowledge of all the laws of the overseas jurisdictions. However, they should have a general understanding of the relevant legal system and cultural norms in each country in which the relevant organisation operates and they should seek to ensure that the organisation has developed policies, processes and procedures to assure regulatory and legal compliance in each of those countries.

What are the main legal systems and corporate governance codes?

At a basic level, a director should have a sound general understanding of the legal system in each the countries in which his or her company is operating.

Some of the major systems include:

- **Common law** (most English-based legal systems including UK, NZ, USA, Canada, India, Singapore, Malaysia and most former British Empire nations) – a system originating in England with a combination of laws made by the legislature and rules arising from cases decided by the courts.
- **Civil law** (most of continental Europe, much of Asia) – a system based on detailed written codes.

- **Sharia law** (most Islamic countries) – traditional sharia law can range from providing the basis of all law in a country (for example, Saudi Arabia) to providing a principled backdrop to a country’s laws (for example, Turkey).
- **Communist** – the communist or former communist legal system provides a background framework over which one of the other systems may generally operate (for example, civil law in Vietnam or common law in Hong Kong). An essential feature of most is state ownership of property, state owned enterprises, and strong discretionary powers vested in central and regional government officials or committees, all of which can significantly affect the way business is done.
- **Roman Dutch law** – based on the ancient Roman law and still relevant in places such as South Africa and Indonesia.

With respect to corporate governance codes, although there is a developing alignment of principles at an international level, each country has its own nuances. Many of them will have mandatory requirements for boards which are quite different to Australia (for example, supervisory boards, employee representation on boards, prescribed gender diversity).

A very good collection of corporate governance codes from over 95 countries can be found at the web site of the European Corporate Governance Institute.¹

They offer an almost infinite variety in terms of detail but there are some common features emerging world-wide, including:

- directors’ duties broadly similar to Australia’s fiduciary duties of care and duty of good faith;
- a trend towards having independent directors on boards;
- board accountability for financial statements.

Virtually every stock exchange in the world has some form of listing requirements which are relevant for directors of companies wishing to list on them.²

Are directors always to act just in the interests of the company?

Directors of a company operating in other jurisdictions may find that they may not be required to act just in the best interests of the company, as is generally the case in Australia. In a number of countries, company directors are required to take into account the interests of various stakeholders other than the company itself. An example is in the United Kingdom where the *Companies Act 2006* provides in s 172 (1):

A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to—

- (a) the likely consequences of any decision in the long terminology
- (b) the interests of the company’s employees
- ...
- (d) the impact of the company’s operations on the community and the environment.

In (continental) Europe, directors are often required to act in the interests of a wider corporate interest including employees, suppliers and the local community (for example in Germany, France and Belgium).

The *Company Law of the People’s Republic of China (Revised in 2013)*³ states in article 5 that:

When engaging in business activities, a company shall abide by laws and administrative regulations, observe social morality and business ethics, act in good faith, accept supervision by the government and the public, and bear social responsibilities.

1. European Corporate Governance Institute, 2019, *Codes*, <https://ecgi.global/content/codes>, (accessed 19 September 2019).

2. Wikipedia, 2019, *List of stock exchanges*, https://en.wikipedia.org/wiki/List_of_stock_exchanges, (accessed 19 September 2019).

3. Standing Committee of the National People’s Congress, 2013, *Company Law of the People’s Republic of China (Revised in 2013)*, 28 December, http://www.fdi.gov.cn/1800000121_39_4814_0_7.html, (accessed 19 September 2019).

Governance issues for directors of subsidiary boards

Corporations operating in a foreign jurisdiction often do so through the vehicle of a subsidiary company. In such cases the directors of the subsidiary company must consider how its governance is to be structured and implemented having regard to the interests of the subsidiary company, the holding company and corporate group, the holding company board and the subsidiary company board.

Governance structures vary, usually within the following three streams of approach:

- **Direct control by holding company main board** – corporate governance functions for the subsidiary in practice are undertaken virtually exclusively by the parent corporation and its board, with the subsidiary board having no real responsibilities outside those absolutely required for local compliance. There are governance risks in this model for the parent company, the parent company directors, the subsidiary company and the subsidiary company directors having regard to principles of *de facto* and *shadow* director control.
- **Shared governance control** – the subsidiary's corporate governance is shared between the subsidiary board and the parent corporation and its board, with the parent corporation and its board taking the lead on strategic issues and with the subsidiary board endorsing that lead but taking responsibility for operational and regulatory compliance requirements at a local level. This is a common and viable approach balancing the interests of all parties.
- **Subsidiary board governance control** – the subsidiary's corporate governance is undertaken entirely by the subsidiary board. This is a technically sound approach but its more regimented structure may pose commercial challenges for an active and dynamic corporate group.

The concept of an advisory board in the foreign country might also be explored. The advantages and disadvantages of each of these frameworks is discussed in detail by Kiel, Hendry and Nicholson in *Corporate Governance Options for the Local Subsidiaries of Multinational Enterprises*.⁴

Governance in countries with weak corporate governance?

In most countries, directors may consult with local legal experts, follow the local corporations law and corporate governance codes and use common sense. However, there are a number of extra steps that should be considered when operating in a country with weak corporate governance or where the system of corporate governance is not clear.

The Organisation for Economic Co-operation and Development (OECD) defines weak governance zones as investment environments in which governments cannot or will not assume their roles in protecting rights (including property rights), providing basic public services and ensuring that public sector management is efficient and effective.

Directors should be aware of the OECD *Risk Awareness Tool for Multinational Enterprises in Weak Governance Zones*.⁵ This tool addresses risks and ethical dilemmas that corporations are likely to face in such zones, including:

- obeying the law;
- observing international instruments;
- heightened care in managing investments;
- knowing business partners and clients;
- dealing with public sector officials; and
- speaking out about wrongdoing.

Also, the International Corporate Governance Network (ICGN) offers *ICGN Guidance on Anti-corruption Practices*, which includes a checklist for investors which can be adapted by boards to ensure management has a strong framework to manage corruption risks.⁶

Corruption and bribery issues and risks

What may be regarded as a perfectly normal way of doing business in one country may be a criminal offence in another. Due to the risks involved, directors need to think about their own personal position on how their organisation should operate and consider what are the organisation's values and standards.

Transparency International produces a corruption perception index each year, which ranks countries according to how corrupt their public sector is perceived to be.⁷

4. G Kiel, K Hendry and G Nicholson G, 2006, "Corporate governance options for the local subsidiaries of multinational enterprises", *Corporate Governance: an international review*, 14(6), pp 568-576, Blackwell Publishing, <http://eprints.qut.edu.au/5076/1/5076.pdf>, (accessed 23 September 2019).

5. Organisation for Economic Co-operation and Development, 2006, *OECD Risk Awareness Tool for Multinational Enterprises in Weak Governance Zones*, OECD Publishing, France, <https://www.oecd.org/daf/inv/corporateresponsibility/36885821.pdf>, (accessed 23 September 2019).

6. International Corporate Governance Network, 2012, *ICGN Guidance on Anti-Corruption Practices: Influencing, Connecting, Informing*, ICGN, https://www.icgn.org/sites/default/files/ICGN_Anti-Corruption_2015_0.pdf, (accessed 23 September 2019).

7. Transparency International, 2018, *Corruption Perceptions Index 2018*, <https://www.transparency.org/cpi2018>, (accessed 23 September 2019).

There are strong anti-bribery laws in many countries, including Australia. Division 70 of the Australian *Criminal Code Act 1995* (Cth) makes it a criminal offence to bribe a foreign public official with a penalty of 10 years imprisonment. It is not possible to argue that you did not realise the conduct constituted bribery. There is an exception where a benefit is a facilitation payment. To satisfy this exception, the benefit must be of minor value and be offered for the sole or dominant purpose of expediting or securing performance of a routine government action of a minor nature and it must be recorded. A routine government action does not include any decision to award or continue business or any decision related to the terms of new or existing business. There are also prescriptive procedural requirements to satisfy if a facilitation payment exception is sought to be relied upon. In addition, the laws of a number of other major countries (for example, the UK) which purport to have extra territorial reach do not recognise a facilitation payment exception.

Most countries have sanctions against bribery of officials – for example, in Australia’s near Asian region, Hong Kong (Prevention of Bribery Ordinance), India (Prevention of Corruption Act), Malaysia (Malaysian Anti-Corruption Commission Act), Philippines (Anti-graft and Corrupt Practices Act), Singapore (Prevention of Corruption Act), Vietnam (Law on Anti-corruption) and China (Criminal Code).

In the United Kingdom, the Bribery Act 2010 carries penalties of 10 years imprisonment for an individual, and unlimited fines for a company. Of particular concern is section 7 (‘Failure of commercial organisations to prevent bribery’) which provides that a relevant commercial organisation is guilty of an offence if a person associated with the organisation bribes another person intending to obtain or retain business for the organisation. It is a defence for the organisation to prove that it had in place adequate procedures designed to prevent persons associated with the organisation from undertaking such conduct. Australian directors should be aware that the definition of relevant commercial organisation to which the Act applies includes ‘any body corporate which carries on a business, or part of a business, in any part of the United Kingdom’. In contrast to the Australian law, there is no exception in relation to ‘facilitation payments’.

The United States Foreign Corrupt Practices Act prohibits any company which is incorporated, or has its principal place of business in the USA, or is a foreign company with US securities on issue or registered in the USA, or any US citizen or resident, from making a corrupt payment (a payment to secure or retain a contract) to a foreign official. Many major corporations have fallen foul of this legislation.

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For more information **t: 1300 739 119** **w: companydirectors.com.au**

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