MALAYSIA

# CORPORATE GOVERNANCE

## DRIVING VALUE CREATION IN ASIA-PACIFIC

Corporate Governance in Malaysia:

# EXCEEDING EXPECTATIONS

*By Mak Yuen Teen*

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# Foreword

**EquitiesFirst™** has joined forces with **Nasdaq Governance Solutions** to publish a series of research reports on corporate governance for selected markets in Asia-Pacific. We have assembled a team of experts on corporate governance in each of the subject markets to provide background and key insights on the space. These reports are for both investors in and management of listed companies focused on creating long-term value in their enterprises.

The topic areas will range from governance best practices, technological shifts, regulatory trends, communication, investor expectations and other topics tailored specifically to each of the regions.

## About the Author

Mak Yuen Teen is Professor (Practice) of Accounting at the NUS Business School and a former Vice Dean of the School. He holds First Class Honours, Masters and PhD degrees in accounting and finance, and is a fellow of CPA Australia. Prof. Mak founded the first corporate governance center in Singapore in 2003 at the NUS Business School and was a member of the Governing Council of the Singapore Institute of Directors.

Prof. Mak served on the Corporate Governance Committee which released Singapore's first Code of Corporate Governance for listed companies in 2001, the Council on Corporate Disclosure and Governance (CCDG) which prescribed accounting standards and revised the Code in 2005, and the Corporate Governance Council which released the fourth version of the Code in 2018. He is currently a member of the Corporate Governance Advisory Committee set up by the Monetary Authority of Singapore (MAS).

He developed the Governance and Transparency Index, now called Singapore Governance and Transparency Index, and was the Singapore representative to develop the ASEAN CG Scorecard. In 2017, he launched the first governance index for REITs and business trusts in Singapore, called GIFT.

In 2014, he received the Corporate Governance Excellence Award from the Securities Investors Association (Singapore) for his contributions to improving corporate governance in Singapore. The following year, he received the Regional Recognition Award for CG Contribution from the Minority Shareholders Watchdog Group and was recognized by the Singapore Institute of Directors as a Corporate Governance pioneer.

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## About EquitiesFirst

EquitiesFirst is a global investment firm, specializing in equity-backed lending. For nearly 20 years, we have provided innovative capital solutions to investors which can be vital or transformative. We work exclusively with corporate leaders, founders and other long-term investors. These stakeholders are united by a common interest in the continued growth and maturation of their underlying businesses. This is the essential objective of good corporate governance. It is our ambition that this research project can serve as a key resource and reference for our partners who engage meaningfully with these topics on a daily basis.

## About Nasdaq Governance Solutions

Nasdaq Governance Solutions, a business of Nasdaq, Inc., offers an integrated suite of governance technology and consultative solutions designed to advance governance excellence worldwide. Through its Nasdaq Boardvantage board portal and collaboration solution and its board and management evaluations and assessment tools, the resources from Nasdaq Governance Solutions help governance professionals organize, streamline, and manage boardroom processes and requirements.

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# Executive Summary

Rankings of corporate governance of Asian markets by the Asian Corporate Governance Association over the past two decades have placed Malaysia between the fourth and the seventh. The recent 1MDB scandal and political upheavals reversed an upward movement in recent years, resulting in a joint fifth ranking among 12 Asian markets in the latest ranking.

However, a closer analysis suggests that the regulatory framework and corporate governance for issuers listed on the Malaysian stock exchange are better than commonly perceived. Corporate governance reforms are guided by roadmaps and specifically target corporate governance problems identified through regulatory reviews. Rules are often prescriptive and there is high compliance. Enforcement for breaches in rules and regulations committed by listed issuers is better than some higher-ranked markets.

However, realization of the full benefits of good corporate governance requires that companies move away from a "box-ticking" mindset. The challenge and priority, like for many other markets, is the implementation of the substance and spirit of good corporate governance to enhance the long-term value of companies for all stakeholders. Poor government and public governance have held back Malaysia in achieving its full potential in corporate governance.

This paper examines the evolution of corporate governance in Malaysia over the last 20 years, the current state of corporate governance, recent developments and what is needed for Malaysia to move beyond compliance.

Some key takeaways from this paper are:

- In general, corporate governance rules and guidelines in Malaysia are relatively stricter and more prescriptive than in many other markets.

- There has been clear progress in the adoption of corporate governance best practices, such as separation of CEO and Chairman roles and number of independent directors (IDs).

- Malaysia is one of the most progressive markets in promoting gender diversity in Asia.

- With a two-tier vote requirement for IDs who have served more than 9 years and a mandatory 12-year limit for IDs to be introduced, the days of long-serving IDs on Malaysian boards are coming to an end. This can help further improve independence, competencies and renewal on boards.

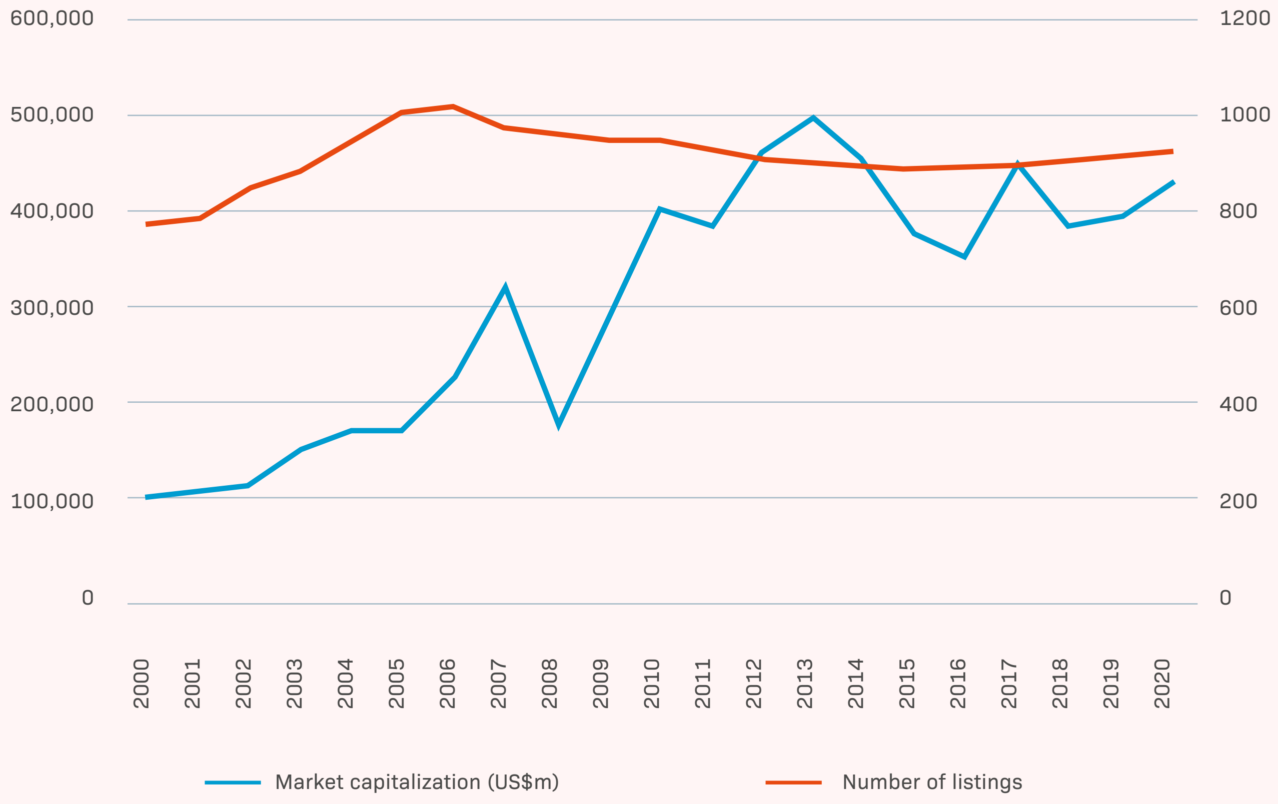
- Areas of improvement remain in terms of age diversity and director selection processes.

# Introduction

The Kuala Lumpur Stock Exchange was demutualized and became Bursa Malaysia (BM) in 2004, and listed in March 2005. Malaysia is among the 27 markets in the MSCI Emerging Markets Index.[1]

Between 2000 and 2006, the number of listings on BM increased from fewer than 800 to more than 1,000. However, like many other exchanges, the number of listings has declined in recent years. As of June 2021, there were a total of 937 listed issuers, with a total market capitalization of about US$420 billion.[2]

**FIG. 1: NUMBER OF LISTINGS AND MARKET CAPITALIZATION FOR BURSA MALAYSIA[2]**




1. https://www.msci.com/home
2. World Federation of Exchanges (The data was retrieved on July 8, 2021) https://statistics.world-exchanges.org

# Listing Segments

There are three market segments on BM –Main Market, ACE Market and LEAP Market. The 937 listed issuers comprise 761 on the Main Market, 138 on the ACE Market and 38 on the LEAP Market.[3] Only seven are foreign listings, with just one being a secondary listing.

The ACE Market, short for Access, Certainty and Efficiency (ACE) Market, is similar to AIM in London and Catalist in Singapore, being a sponsor-based regime. However, unlike the two latter markets, an ACE Market issuer is only required to continue to have a sponsor for at least three full financial years after listing or at least one full financial year after it has generated operating revenue, whichever is later. It needs only to retain a sponsor for one full financial year after listing on the ACE Market if the sponsor confirms that the issuer meets the quantitative criteria for admission to the Main Market.

The LEAP Market – or the Leading Entrepreneur Accelerator Platform (LEAP) Market - is intended especially for small-medium enterprises. It is an adviser-driven market accessible only to sophisticated investors. Public companies registered in Malaysia can choose to seek a primary listing on the LEAP Market provided that they have a comprehensive business plan. A profitable track record, however, is not necessary.

In Malaysia, there are three public pension funds, with two investing in equities. These two pension funds, however, are not allowed to invest in ACE or LEAP companies due to high risks.

**Malaysia formed the High-Level Finance Committee on Corporate Governance and in 2000, became the first ASEAN market to introduce a corporate governance code.**

3. Bursa Malaysia (The information was retrieved on July 8, 2021) https://www.bursamalaysia.com/

# Evolution of Corporate Governance

After the East Asian financial crisis, Malaysia formed the High-Level Finance Committee on Corporate Governance and in 2000, became the first ASEAN market to introduce a corporate governance code, the Malaysian Code on Corporate Governance (MCCG).

The MCCG, which is issued by the Securities Commission (SC), was subsequently revised in 2007, 2012, 2017 and 2021. A significant revamp was made in 2017 when, in order to emphasize the importance of implementing the substance and spirit of recommended best practices, the approach was changed from "Comply or Explain" to "Comprehend, Apply and Report" – or CARE in short. Under the CARE approach, companies which do not follow recommended best practices have to explain how alternative practices they adopt achieve specified intended outcomes. Further, higher standards were imposed on large companies, defined as those in the FTSE/Bursa Top 100 Index or with a market capitalization of RM2 billion or more. Larger companies were also expected to eventually adopt all recommended practices and to specify timelines for doing so. "Step up" practices - aimed particularly at large companies - were also added to encourage companies to strive for excellence.

The latest version of the MCCG released in April 2021 retained the changes introduced in 2017 but added new best practices and guidance to:

a. improve board policies and processes including those related to director selection, nomination and appointment;

b. strengthen board oversight and the integration of sustainability considerations in the strategy and operations of companies; and

c. encourage the adoption of best practices, particularly those found to have relatively lower adoption based on the SC review. Some specific changes include extending the recommendation of at least 30% of female directors from large companies to all companies; restrictions on board chairmen serving on key board committees; annual two-tier voting for independent directors tightened from after 12 years to after 9 years; and listed companies discouraged from appointing active politicians to their boards.

In June 2020, BM amended its rules to require all listed issuers to publish on their websites their policy on anti-corruption, and policies and procedures on whistleblowing. This follows amendments to Malaysia's anti-corruption law which came into effect that same month, which imposes corporate liability for corruption committed by a broad range of persons associated with a commercial organization, unless the organization can prove that it had in place adequate procedures to prevent corruption. Under the new provision, senior personnel such as directors and officers also have personal criminal liability. Prior to this, Malaysia had introduced the Whistleblower Protection Act 2010 to protect those who report wrongdoing in both the private and public sectors to an enforcement agency.

BM has also announced that independent directors (IDs) will not be allowed to serve as an ID on the same board for more than nine years. A consultation paper was issued in July 2021 on the implementation of this new rule and rules requiring listed issuers to develop, publish and implement a "fit and proper" policy for directors.

In general, corporate governance rules and guidelines in Malaysia are relatively stricter and more prescriptive than in many other markets, and rule changes are targeted at corporate governance issues identified through regulatory reviews. This indicates a willingness on her part to adopt measures to improve corporate governance and protect investors that are stricter than those in other markets.

Malaysia has also adopted a strategic approach in its corporate governance reform agenda. In July 2011, the SC released a "Corporate Governance Blueprint 2011" as a key part of the master plan to "expand the role of the capital market in invigorating national economic growth". The blueprint sets out reform priorities and responsibilities for different stakeholders to drive improvements in corporate governance. This was followed by the report "Corporate Governance Strategic Priorities 2017-2020" also released by the SC. In April 2020, the SC established the Corporate Governance Council (CG Council), which brings together key corporate governance stakeholders to provide strategic direction for the development of corporate governance policies and initiatives for the capital market and to coordinate its implementation.

# Regulatory Bodies

The key regulatory bodies in Malaysia applicable to listed issuers include:

a. Bursa RegSub, which was set up in February 2020 as a wholly-owned regulatory subsidiary of BM with a separate board of directors, and is responsible for enforcing the listing rules;

b. SC, which is responsible for administering the Capital Markets and Services Act, Malaysia's version of securities legislation, and enforcing compliance with accounting standards by listed issuers;

c. Audit Oversight Board (AOB), a unit within the SC which is responsible for overseeing external auditors, including registration, inspection and enforcement;

d. Companies Commission of Malaysia (CCM), which is responsible for the incorporation of companies and registration of businesses, and enforcing the Companies Act; and

e. other regulatory authorities responsible for investigating and prosecution of serious offenses under the various statutory rules. In addition, Bank Negara Malaysia (BNM) regulates financial institutions, whether listed or unlisted.

With effect from July 2020, new guidelines introduced by the SC allow it to impose sanctions on directors of listed issuers and their subsidiaries who breach their fiduciary duties. This is expected to improve the enforcement of breaches of fiduciary duties which has in the past been the responsibility of the CCM.

The establishment of a separate regulatory subsidiary under BM follows the trend in some other markets, such as Singapore, the aim being to enhance the independence of the regulatory function within the stock exchange.

However, whether this will make a difference to enforcement outcomes is unclear as the subsidiary is still part of BM and therefore the conflict between commercial and regulatory objectives may not necessarily be resolved. That being said, one thing which has often been overlooked is that BM has been quite active in taking enforcement actions against directors for breaches of listing rules. Between 2014 and 2020, it publicly reprimanded and imposed fines totaling RM32.4 million on 179 directors, and publicly reprimanded another 42 directors without a fine.[4]

**To enhance the independence of the regulatory function within the stock exchange**

4. Mak,Y.T. .(2021, June 8). Corporate Governance Ranking Improves for Singapore. The Business Times.

# Market Institutions

The current incarnation of the peak body for company directors in Malaysia - the Institute of Corporate Directors Malaysia (ICDM) - was officially launched in October 2018. Prior to this, the Malaysian Alliance of Corporate Directors (MACD) was established in 2009, which remains in existence today.

An essential part of being an effective director is professional education, both as a first-time director and on a continuing basis. For Malaysia, all first-time directors must attend BM's 1.5-day Mandatory Accreditation Programme (MAP) within four months of becoming a director. There are no exemptions, including directors who have served on boards of listed companies in other countries. From 2018 until June 2021, a total of 1,878 first-time directors have attended the MAP. This indicates that each year, more than 500 first-time directors join the boards of listed issuers in Malaysia. This is partly driven by regulatory initiatives such as term limits on IDs and minimum percentage of female directors, and is a healthy sign that the pool of qualified directors is constantly being expanded and there is board renewal taking place.

Malaysia has two major investor bodies which are focused on corporate governance. The Minority Shareholders Watch Group (MSWG) was established in 2000 primarily to protect minority investors through shareholder activism. It acts as a collective voice for retail and institutional minority shareholders and has since evolved into an independent research organization on corporate governance matters. It also advises on voting at general meetings of Malaysian listed companies.

The other investor body in Malaysia is the Institutional Investors Council (IIC), formed in July 2015 following the launch of the Malaysian Code for Institutional Investors (MCII) in 2014. It serves as a platform to, among others, encourages the effective adoption of the MCII and for collective engagement with companies. Currently, there are 37 institutional investors and asset managers who are signatories to the MCII and 26 members of the IIC. MSWG collaborates closely with the IIC, with the former acting as the Secretariat to the latter.

**Malaysia has two major investor bodies which are focused on corporate governance.**

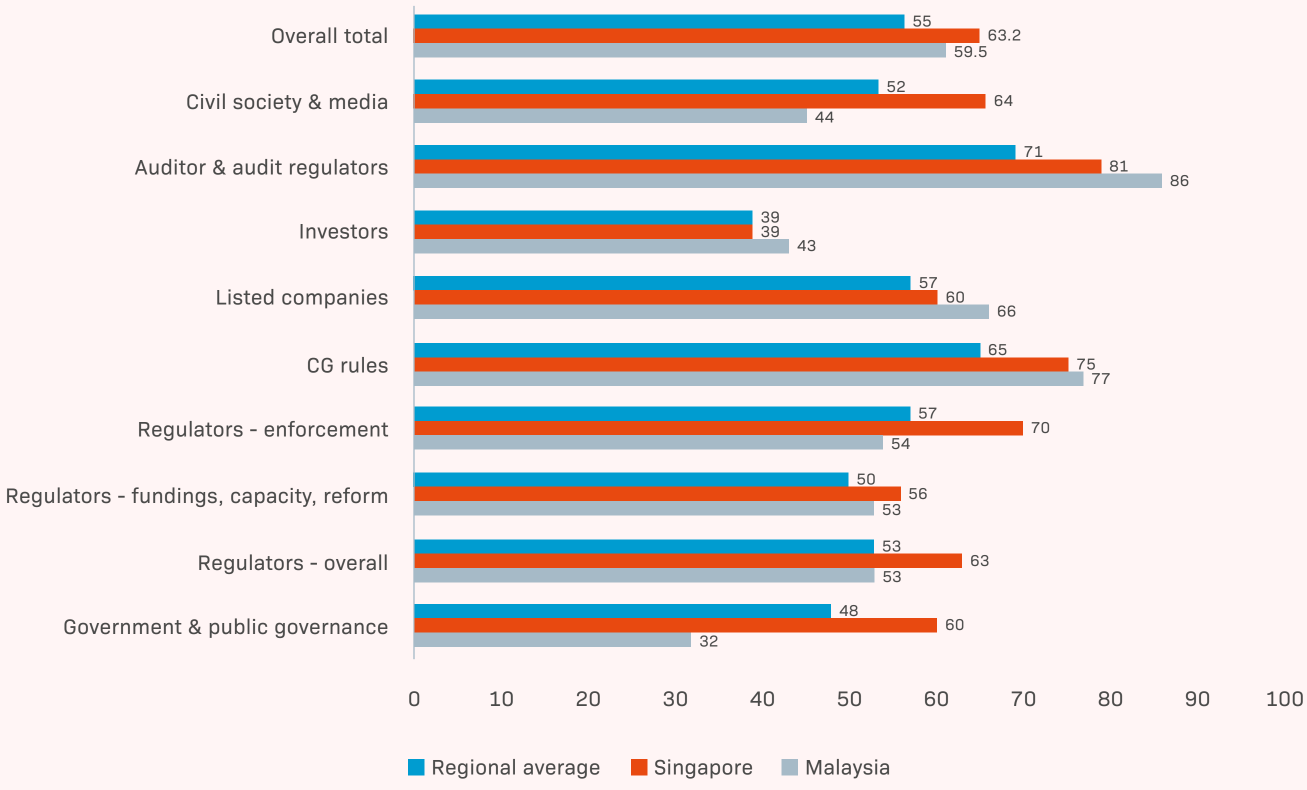
# Overall State of Corporate Governance

Although Malaysia started its corporate governance journey more than 20 years ago, it was the first ASEAN market to introduce a corporate governance code and has continued to introduce reforms, the rankings published by the Asian Corporate Governance Association (ACGA) has consistently ranked Malaysia only between fourth and seventh out of up to 12 Asian markets. The recent 1MDB scandal and political upheavals also reversed a recent upward movement, resulting in a joint fifth position in the latest ranking.

FIG. 2 shows how Malaysia was ranked by ACGA in 2020, compared to Singapore and the region, in areas relevant to the quality of corporate governance in a market. Malaysia significantly underperforms Singapore on Government & Public Governance, Regulators, and Civil Society & Media, but slightly outperforms Singapore on Corporate Governance Rules, Listed Companies, Investors and Auditors & Audit Regulators. Compared to the region, Malaysia significantly underperforms on Government & Public Governance and Civil Society & Media and is comparable on the three aspects of Regulators, but outperforms on an overall basis. The ACGA ranking reinforces that poor government and public governance weigh down assessments and perceptions about Malaysia's overall state of corporate governance.

The two Malaysian public pension funds which invest in Malaysian issuers listed on the Main Market are active in engagement and voting. Domestic institutional investor activism by local pension funds that we see in many developed markets is present and developing in Malaysia.

**FIG. 2: CG WATCH 2020 SCORES BY CATEGORY FOR MALAYSIA COMPARED TO SINGAPORE AND THE REGION[5]**

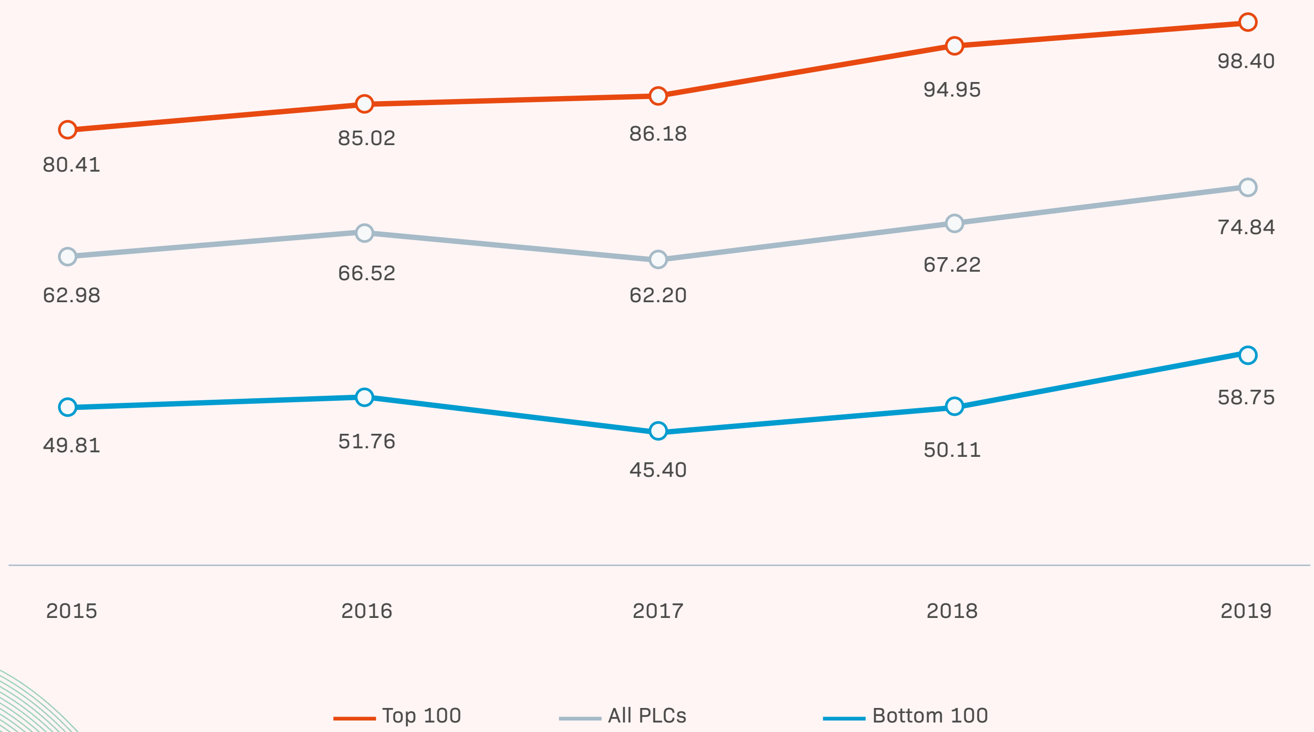



5. Asian Corporate Governance Association (ACGA), CG Watch https://www.acga-asia.org/cgwatch.php

The MSWG publishes an annual report each year which shows how Malaysian listed issuers fare on overall corporate governance disclosures and in specific areas. Since 2012, it has used the ASEAN CG scorecard developed under the auspices of the ASEAN Capital Markets Forum to assess disclosures. FIG. 3 shows how those which were rated as among the top 100 in disclosures, the bottom 100 and all listed companies, have performed between 2015 and 2019. Overall, there is an upward trend for all three groups. However, disclosures may not reflect actual practices and therefore the trend should be interpreted with caution.

To encourage the adoption of best practices and track the adoption of the MCCG, the SC has since 2019 published an annual Corporate Governance Monitor (CGM) report[7]. The latest CGM in 2020 covered 868 listed companies. The CGM is used by the SC to inform its review of corporate governance rules to determine if changes are needed to further raise standards.

**FIG. 3: TRENDS IN OVERALL CORPORATE GOVERNANCE DISCLOSURES FOR MALAYSIAN LISTED COMPANIES[6]**




6. Minority Shareholders Watch Group, Malaysia-ASEAN Corporate Governance Report 2019
7. Securities Commission Malaysia. (n.d.). Corporate Governance https://www.sc.com.my/regulation/corporate-governance

# Implementation of Key Corporate Governance Practices

In general, Malaysian companies have made good progress in adopting corporate governance best practices. However, investors should exercise caution when interpreting statistics on adoption because they do not necessarily equate to the implementation of the spirit and substance underlying these practices. For example, companies which have more directors who are classified as IDs may not necessarily have truly independent or more effective boards.

## Separation of Chairman and CEO Roles

Like most corporate governance codes around the world, the MCCG recommends that companies separate the roles of the Chairman and CEO. Since the board's role is to oversee management and operations, separating the roles of the Chairman and CEO will better ensure that the board is able to do so objectively. Ideally, the Chairman should be an independent director. The ISS ESG Governance QualityScore developed by Institutional Shareholder Services, the largest proxy advisory firm in the world, indicates that an Independent Chairman is broadly considered a best practice and applicable to all regions.[8]

Similarly, Glass Lewis, the second-largest proxy advisory firm, takes the view that "shareholders are better served when the board is led by an independent chair".[9]

As FIG. 4 shows, the percentage of Malaysian companies which separated the roles increased from about 75% in 2015 to peak at more than 85% in 2017 and then declined to around 76%.[6] The percentage of companies with an Independent Chairman has remained relatively stable at just under half. More can be done to encourage companies to appoint independent chairmen. By way of comparison, only 6.9% of FTSE 350 UK companies did not have a chair who was independent on appointment in 2020.[10] In Canada, about 61% of the 100 "blue chip" companies in the CSSBI 100 have an Independent Chairman.[11] A 2007 study of the top 100 listed companies in Australia found that 78.4% had an Independent Chairman.[12] In the U.S., where CEOs have traditionally also held the Chairman's role, 34% of S&P 500 companies have appointed an Independent Chairman in 2020, compared to 19% a decade ago.[13]

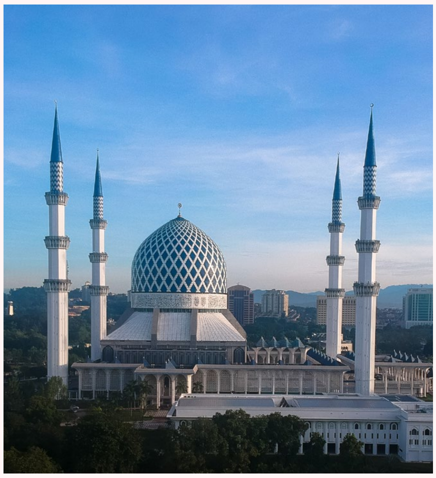
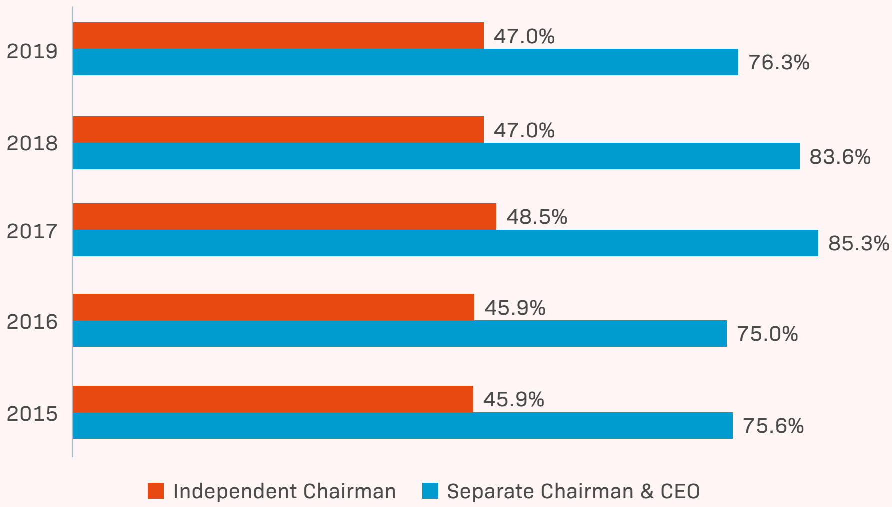


**FIG. 4: TRENDS IN SEPARATION OF CHAIRMAN AND CEO ROLES AND APPOINTMENT OF INDEPENDENT CHAIRMAN IN MALAYSIA[6]**




8. Institutional Shareholder Services. (2021, June 30). ISS ESG Governance QualityScore https://www.issgovernance.com/file/products/qualityscore-techdoc.pdf
9. Glass Lewis. (2021, March). Independent Chair http://www.glasslewis.com/wp-content/uploads/2017/03/2017-In-Depth-Independent-Chair-marked-copy-2.pdf
10. Grant Thornton. (2020). Corporate Governance Review 2020 https://www.grantthornton.global/globalassets/1.-member-firms/global/insights/article-pdfs/2020/uk-corporate-governance-review-2020.pdf
11. SpencerStuart. (2020). 2020 Canada Spencer Stuart Board Index https://www.spencerstuart.com/-/media/2021/march/canadabi/canada-board-index-2020.pdf
12. Australian Council of Super Investors Inc. (2007). Board Composition and Non-Executive Director Pay in the Top 100 Companies: 2007. Research Paper Prepared by ISS Governance Services https://www.pc.gov.au/inquiries/completed/executive-remuneration/submissions/sub071-attachment2.pdf
13. SpencerStuart. (2020). 2020 U.S. Spencer Stuart Board Index https://www.spencerstuart.com/-/media/2020/december/ssbi2020/2020_us_spencer_stuart_board_index.pdf

## Independent Directors

BM's listing requirements mandate that at least two directors or one-third of the board, whichever is higher, must be IDs. This requirement has long been in place. The MCCG recommends that large companies have a majority of IDs, while other companies have at least half of the board being IDs. As of 2019, 64% of Malaysian companies have at least half of the board made up of IDs (FIG. 5). The Malaysian Board Practices Review 2020 (MBPR), based on a survey of 104 listed issuers, found that 72% have at least half of the board made up of IDs.[14]

While Malaysia has made good progress based on the percentage of companies having half or more IDs on their boards, what is more important is that IDs are truly independent and competent. Other recent regulatory initiatives such as tenure limits, board diversity, objectivity and transparency of the director search and nomination process, and fit and proper criteria for directors, are steps in the right direction to achieving more independent and effective boards.

## Board Diversity

Malaysia surprises many for being one the most progressive in promoting gender diversity in Asia. It was one of the first markets in Asia to set a specific target on the percentage of female directors on listed boards, with the announcement of a 30% target in 2011 to be achieved by 2016. In 2015, the 30% Club Malaysia was launched to improve the gender imbalance on boards in Malaysia.

The percentage of listed company directorships held by women increased from 9.9% in 2015 to 15% in 2019 (FIG. 6), which while an improvement, was well below the 30% target that was set.

To continue the push for improved gender diversity, the MCCG 2017

**FIG. 5: TREND IN PERCENTAGE OF INDEPENDENT DIRECTORS IN MALAYSIA[6]**

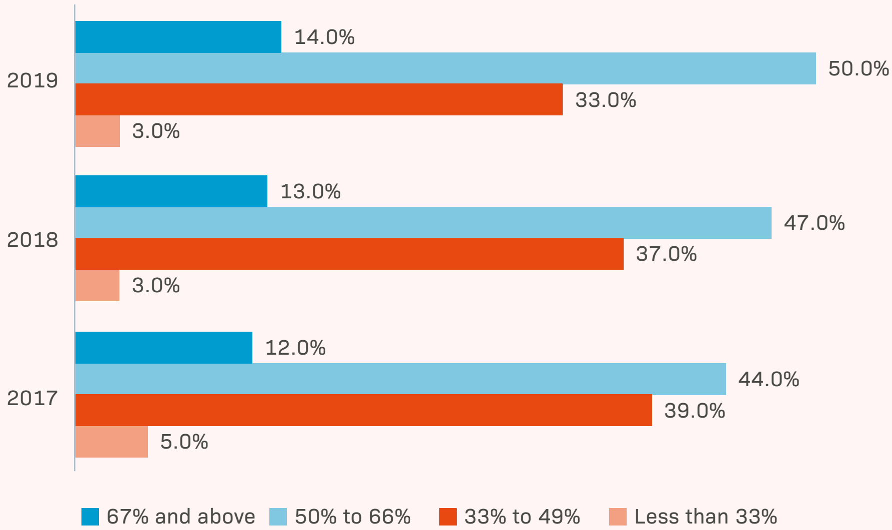
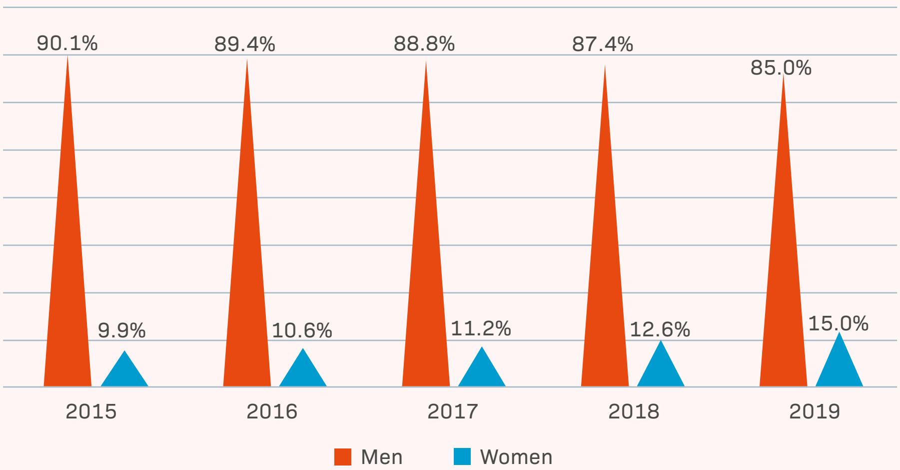


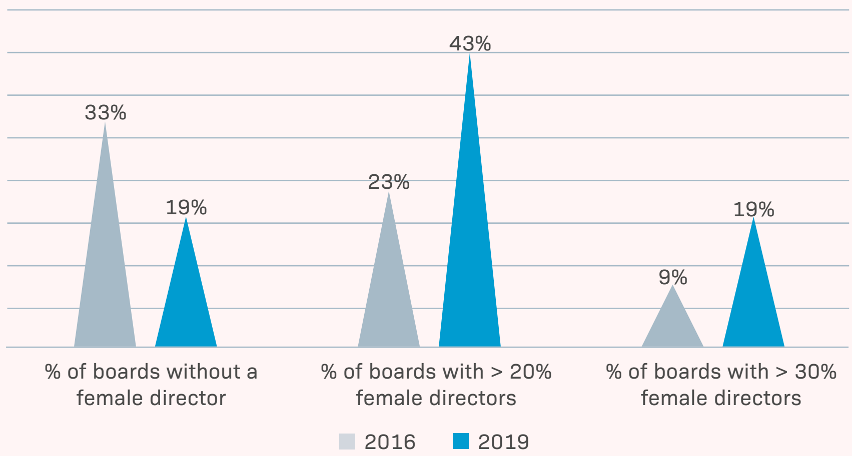

**FIG. 6: TREND IN PERCENTAGE OF FEMALE DIRECTORS IN MALAYSIA[6]**




14. Institute of Corporate Directors Malaysia, Russell Reynolds Associates and Bursa Malaysia, Malaysian Board Practices Review 2020, 2021.

stated that large companies were to have 30% of female directors on their boards. The MCCG 2021 has extended it to all companies after a review of the implementation of the MCCG 2017 found insufficient progress in this area. A 2020 report on women board directors in Asia-Pacific found that India, Malaysia and Thailand were behind Australia only in having the lowest percentage of all-male boards among the largest companies, with 90% of these boards having women. The best performing economies in appointing women on boards were Australia with 33.1%, followed by Malaysia with 26.4%, compared to an overall average of 14.8% for Asia-Pacific.[15]

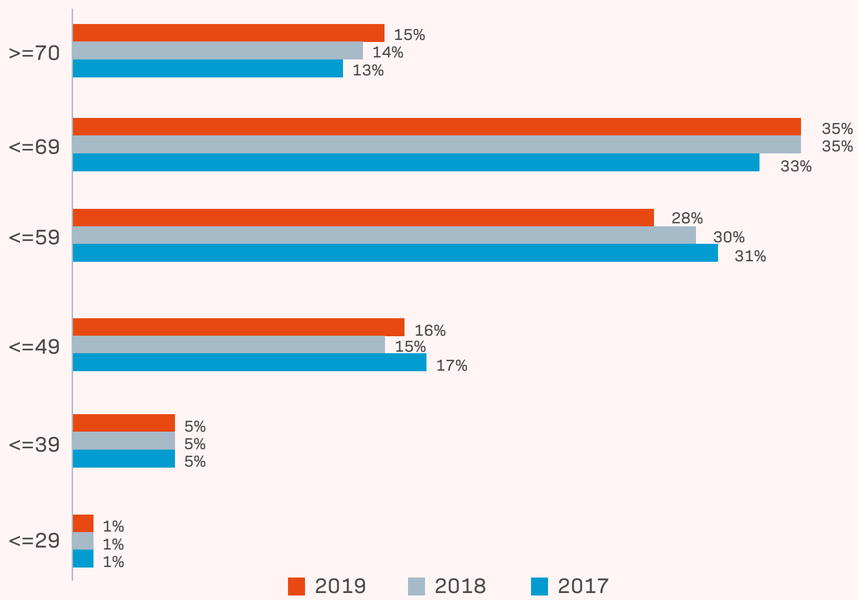
**FIG. 7: TREND IN BOARDS WITH DIFFERENT PERCENTAGES OF FEMALE DIRECTORS IN MALAYSIA[16]**




The Malaysian Board Diversity Study & Index (MBDSI) published by the ICDM, which covered 312 Malaysian listed companies, found that between 2016 and 2019, the percentage of boards without a female director fell from 33% to 19%. The percentage of boards with at least 30% of female directors increased from 9% to 19% (FIG. 7).

In terms of age diversity, there has been a slight increase in the percentage of directors who are aged 60 years or more between 2017 and 2019 based on a recent report by ICDM, with such directors making up 50% of all directors in 2019, compared to 49% in 2018 and 46% in 2017 (FIG. 8). Malaysia boards need to focus on improving age diversity by appointing more directors in the younger age groups who are more likely to have skills and expertise in emerging areas such as digitalization, cybersecurity and sustainability.

**FIG. 8: TREND IN AGE OF DIRECTORS IN MALAYSIA[16]**




## Tenure of Independent Directors

Long tenure can inhibit board renewal and lead to a decline in the relevance of skills and competencies on the board. Regulators in many countries have also identified long tenure as a threat to the independence of IDs, due to familiarity and other risks.

The MCCG 2021 specifies a two-tier vote for independent directors after nine years to continue to be considered independent. This was stricter than the MCCG 2017 which specified a two-tier vote only after 12 years. The first-tier vote is by large shareholders and the second-tier vote is by all other shareholders. A mandatory limit of 12 years for IDs is to be introduced under the listing rules in Malaysia.

FIG. 9 shows the tenure of IDs for Malaysia. The percentage of IDs who had served nine years is 34%, with a recent downward trend. The survey of 104 companies in the MBPR 2020 reported that 19% of IDs had served more than nine years. With the two-tier vote and mandatory 12-year limit for IDs, the days of long-serving IDs on Malaysian boards are coming to an end.

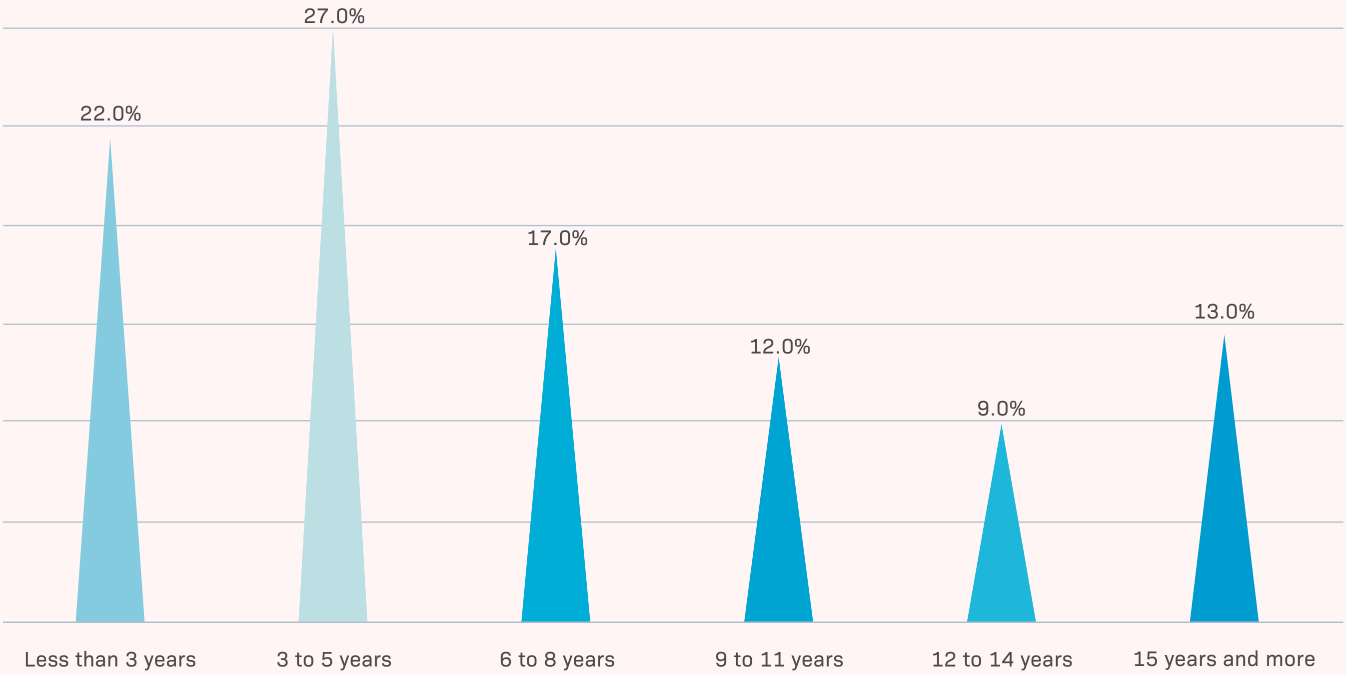
15. Corporate Women Directors International. (2020). 2020 CWDI Report: Women Board Directors of Asia-Pacific. https://globewomen.org/CWDINet/index.php/2018-fortune-global-200-companies-2/
16. Institute of Corporate Directors Malaysia, Malaysian Board Diversity Study & Index, 2021

## Multiple Directorships

For many years, the listing rules in Malaysia have imposed a limit of five listed company directorships that any director can hold. It was one of the first countries to impose a specific limit. As a result, the issue of busy directors or "overboarding" is less of a concern in Malaysia than in many other markets.

> **Investors should look for companies that go beyond mere compliance by considering other indicators and engage with boards and management of companies**

**FIG. 9: TENURE OF INDEPENDENT DIRECTORS IN MALAYSIA (2019)[6]**




# Enhancing Board Effectiveness

Malaysia has introduced many reforms which have improved the board composition of companies, such as separation of Chairman and CEO, increasing the percentage of IDs, improving gender diversity, restricting the tenure of IDs and limiting the number of directorships an individual can hold. BM also plans to introduce rules requiring companies to develop, publish and implement a fit and proper policy for directors.

While much has been done to improve board composition, other factors such as board decision-making processes and board culture are also critical for board effectiveness. In order for corporate governance to create long-term value for all stakeholders, companies must do more than "tick boxes" on prescribed corporate governance practices. Investors should look for companies that go beyond mere compliance by considering other indicators, and engage with boards and management of companies to assess factors such as how boards make decisions and whether there is an appropriate board culture that encourages constructive and rigorous debate.

## Board Meeting Frequency

Boards that meet infrequently may not be adequately discharging their oversight responsibilities and adding value, although the number of board meetings is only one indicator of a board's engagement with the company and boards that meet too frequently under normal circumstances may be interfering with day-to-day management.

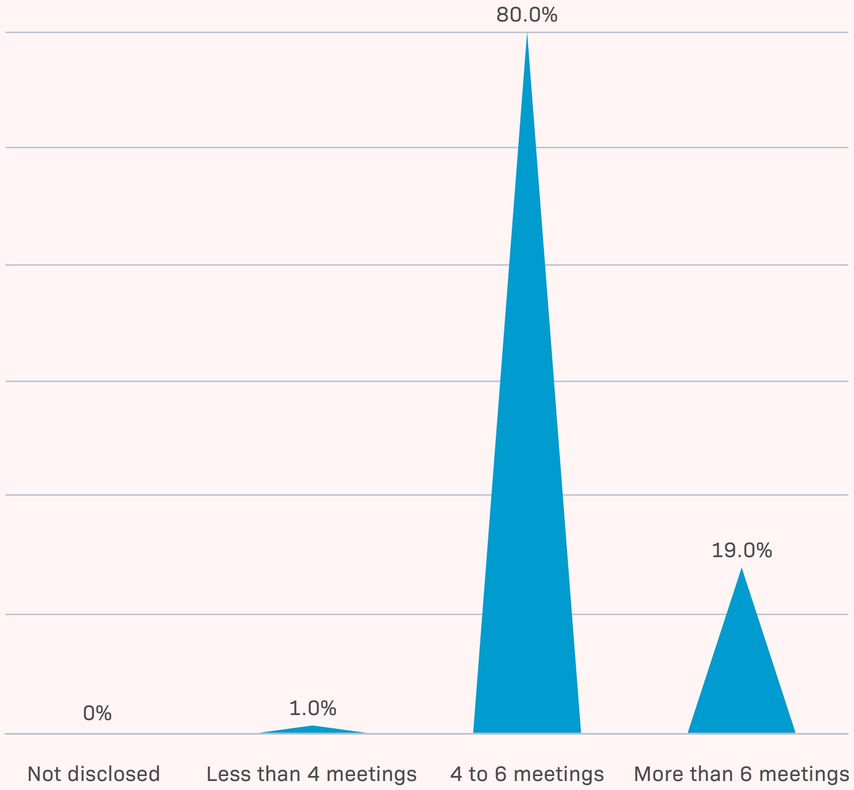
Nearly all Malaysian boards meet at least four times a year, with about 1 in 5 boards meeting more than 6 times (FIG. 10). While boards meeting an average of once every quarter or two months is comparable to many other boards in more developed markets, what is also important are the matters discussed, whether adequate time is spent discussing strategic issues, and board dynamics and culture.

Investors engaging with boards may want to inquire about time spent on setting and monitoring corporate culture; discussing issues relating to sustainability and broader stakeholders' interests; discussing purpose, strategy and long-term future of the company; and considering key risks, including corruption risks.

## Selection of Directors

Like many other markets, Malaysian companies tend to rely on personal networks to identify candidates for appointment as IDs. The survey of 104 companies in the MBPR 2020 shows that personal network was the most common sourcing method for 74% of

**FIG. 10: NUMBER OF BOARD MEETINGS HELD IN A YEAR FOR MALAYSIAN COMPANIES (2019)[6]**



companies, with independent search institutions being the most common method for only 8% of companies (FIG. 11). Where IDs are sourced mostly from personal networks or nominations by a major shareholder/parent company, there may be questions about their true independence and relevance of their skills and competencies, and whether there will be diversity of thought on the board.

However, while the percentage of companies using independent search institutions such as ICDM, MSWG and professional search firms is currently low, this is likely to improve. ICDM, for example, sends emails informing members about board opportunities which set out requirements on attributes, competencies, experience and prior board experience. A recent email shows that this source is being used particularly to identify suitable female candidates, in line with the emphasis on gender diversity in Malaysia.

Regulators have recognized the importance of companies having a robust search and nomination process for directors. The MCCG 2021 states that in identifying candidates for appointment as directors, the board should not solely rely on recommendations from existing directors, management or major shareholders, and should instead utilize independent sources to identify suitably qualified candidates. It further adds that “if the selection of candidates was based on recommendations made by existing directors, management or major shareholders, the Nominating Committee should explain why these sources suffice and other sources were not used”.

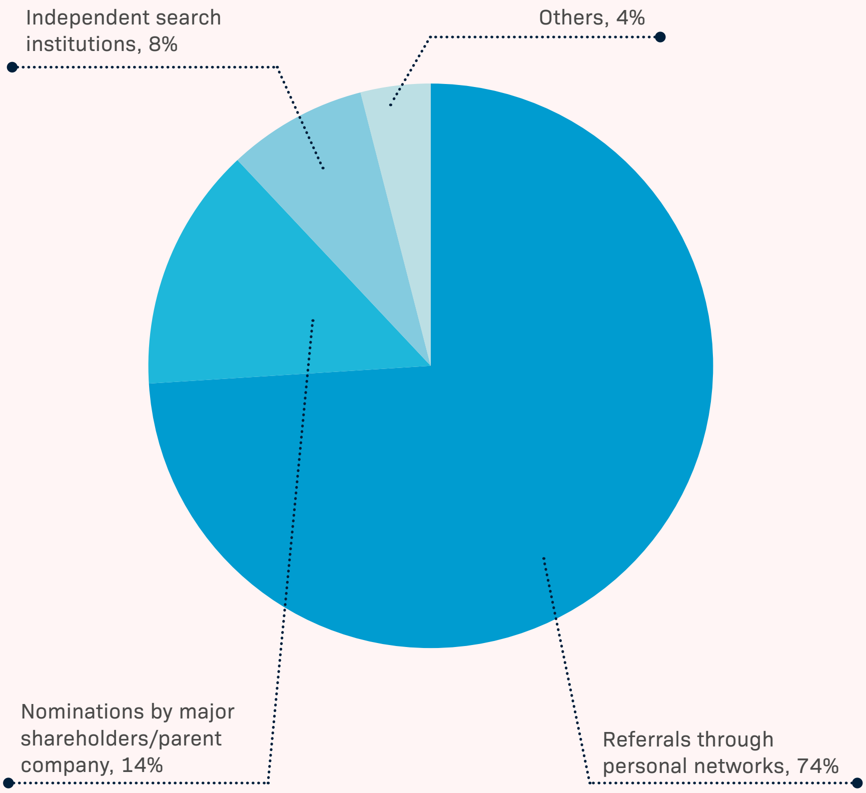
Investors should ask boards about the methods they use to identify potential candidates for appointment as IDs and the due diligence that is done before a candidate is appointed.

They should also ask about the attributes, competencies and experience of candidates companies are looking for to assess if companies are sourcing for directors with less traditional but important backgrounds in areas such as technology; innovation; environmental, social and governance issues; and human capital.

## Other indicators of board effectiveness

Other areas that investors should engage with companies on to assess the effectiveness of their boards include whether directors receive proper induction when they are appointed; participate in professional education programs on an ongoing basis; how performance assessment of boards, committees, individual directors and CEO are conducted; and succession planning of directors, senior management and other critical employees.

**FIG. 11: COMMON SOURCING METHODS FOR INDEPENDENT DIRECTORS FOR MALAYSIAN COMPANIES[17]**




17. Malaysian Board Practices Review 2020

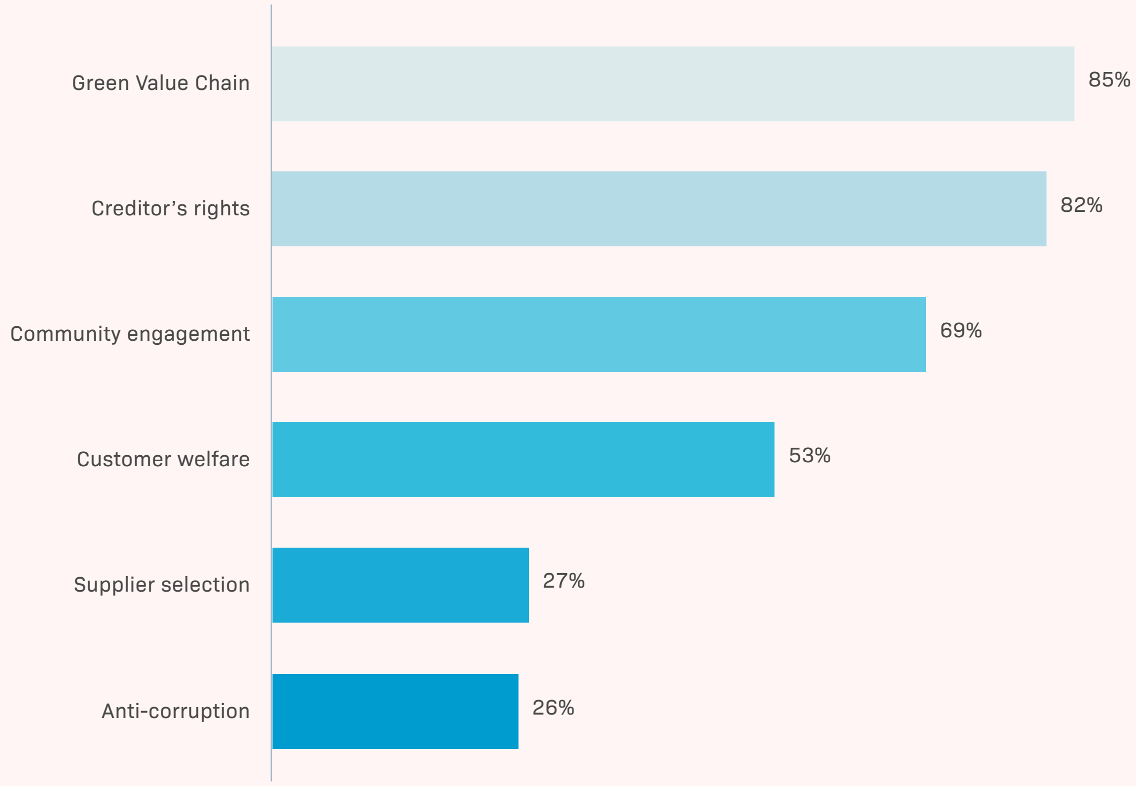
# Moving from Governance to Environmental, Social and Governance (ESG)

Like many other markets, regulators, investors and companies in Malaysia are increasingly focusing beyond governance and on environmental, social and governance (ESG) issues. Sustainability reporting is now mandatory for Malaysian companies.

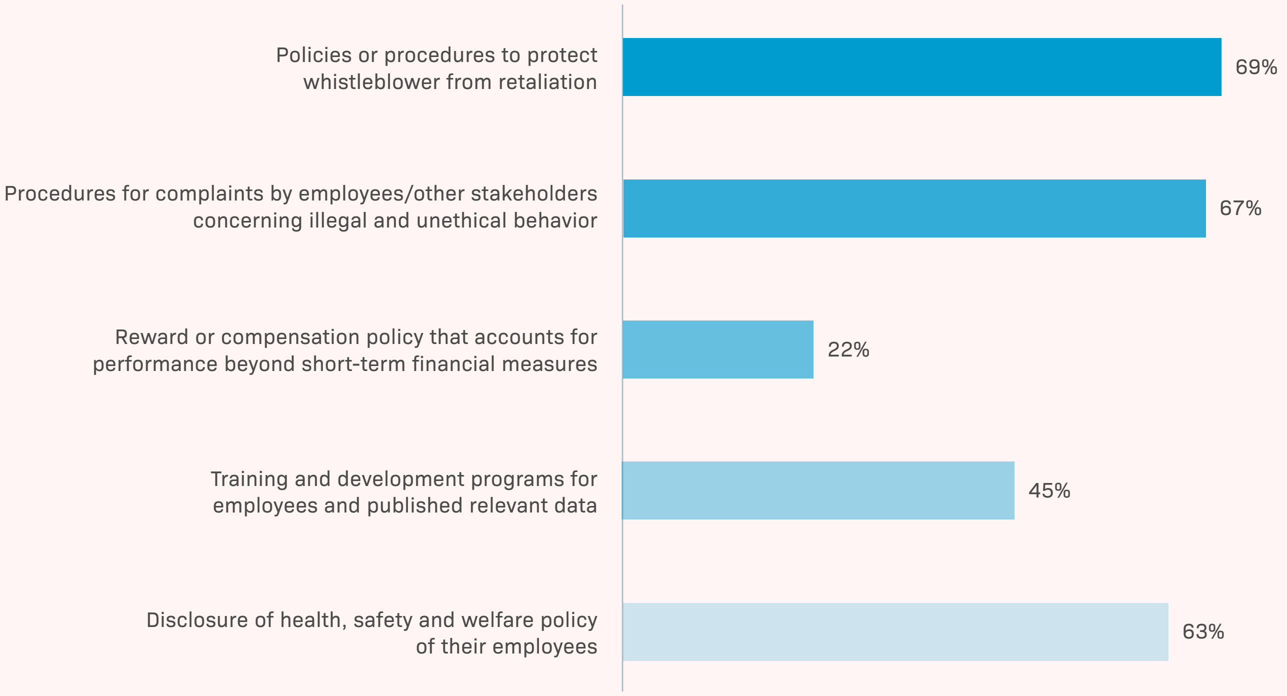
The Malaysia-ASEAN Corporate Governance Report 2019 found that 98.6% of the 866 Malaysian listed issuers published a standalone Sustainability Report or have a separate section on sustainability in their annual reports. The report found that disclosure of policies and practices on a green value chain was the most common, while disclosure on anti-corruption was least common (FIG. 12). However, starting from June 2020, Main Market and ACE issuers in Malaysia must disclose on their website their policy on anti-corruption and policy and procedures on whistleblowing. Therefore, disclosure in this area would be expected to improve considerably.

In the area of employee welfare, the study found that policies and procedures to protect the whistleblower from retaliation; procedures for complaints by employees/other stakeholders to raise concerns; and health, safety and welfare policies for employees are the three areas that are most frequently disclosed by Malaysian issuers (FIG. 13).

**FIG. 12: PERCENTAGE OF MALAYSIAN ISSUERS THAT DISCLOSE POLICIES AND PRACTICES ON DIFFERENT ASPECTS OF STAKEHOLDER RIGHTS**[6]



#### FIG. 13: PERCENTAGE OF MALAYSIAN ISSUERS THAT DISCLOSE POLICIES AND PRACTICES ON DIFFERENT ASPECTS OF EMPLOYEE WELFARE[6]




## Markets, regulators, investors and companies in Malaysia are increasingly focusing beyond governance and on environmental, social and governance (ESG) issues.

# Conclusion

Malaysia has been strategic and progressive in making reforms to its corporate governance rules.

Over the past 20 years, considerable progress has been achieved in compliance with key corporate governance rules and guidelines in Malaysia. Regional rankings of corporate governance of Asian markets have generally put Malaysia somewhere in the middle. A recent major scandal, political instability and allegations of political corruption have hurt how Malaysia fares on these rankings and how it is perceived by the international investor community.

However, as this paper has shown, Malaysia has been strategic and progressive in making reforms to its corporate governance rules. These are informed by regular regulatory reviews designed to address problems that ail the market. It has developed strong regulatory and market institutions and ratcheted-up enforcement for capital market breaches in the past few years.

Based on this writer's personal experience monitoring developments in Malaysia over the last 20 years; engaging with regulators, directors, investors and other stakeholders; and conducting professional education programs for first-time and experienced directors across both listed companies and financial institutions, the reality is quite different from common perceptions about the state of corporate governance in Malaysia. While there is no doubt that political and public governance issues will hurt investor confidence, there are many companies and directors in Malaysia who take good corporate governance seriously.

Capital market regulators are prepared to introduce necessary reforms to enhance investor protection and that is not the same inclination as we observe in some other markets where stock exchanges and regulators lower the bar in order to attract more listings. As with any market, there are companies that are well-governed and managed and those that are not. Investors should carefully assess the corporate governance of companies they invest in. There is cause for optimism that corporate governance will continue to improve in Malaysia.

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