

FINANCE COMMITTEE  
ON  
CORPORATE GOVERNANCE

Malaysian Code on  
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March 2000

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Securities Commission  
No 3, Persiaran Bukit Kiara  
Bukit Kiara  
50490 Kuala Lumpur  
Malaysia  
Tel: 603-654 8000 Fax: 603-651 1818  
Homepage: [Http://www.sc.com.my](http://www.sc.com.my)

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@Finance Committee on Corporate Governance  
March 2000

Perpustakaan Negara Malaysia Cataloguing-in-Publication Data  
The Malaysian code on corporate governance/Finance Committee  
on Corporate Governance.

ISBN 983-9386-23-9

1. Corporate governance-- Law and legislation-- Malaysia
  2. Corporation law--Malaysia
  3. Stockholders--Legal status, laws etc.--Malaysia
  4. Insider trading in securities--Law and legislations--Malaysia.
- I. Malaysia. Suruhanjaya Sekuriti, Jawatankuasa Kewangan Tadbir Urus Koprak.  
346.5950926

# CONTENTS

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	<b>PAGES</b>
<b>INTRODUCTION</b>	1-6
PART 1      PRINCIPLES OF CORPORATE GOVERNANCE	7-8
PART 2      BEST PRACTICES IN CORPORATE GOVERNANCE	9-15
PART 3      PRINCIPLES AND BEST PRACTICES FOR OTHER CORPORATE PARTICIPANTS	16
PART 4      EXPLANATORY	17-47
 <b>APPENDICES</b>	
 JPK WORKING GROUP 1	 48-49
MEMBERSHIP OF THE COMMITTEE	50

# INTRODUCTION

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## 1. The Significance of a Code on Corporate Governance for Malaysia

1.1 The Malaysian Code on Corporate Governance was developed by the Working Group on Best Practices in Corporate Governance (JPK1) and subsequently approved by the high level Finance Committee on Corporate Governance. JPK1 was chaired by the Chairman of the Federation of Public Listed Companies. The members of the JPK1 comprise a mix of private and public sector participation. A list of the members of JPK1 is set out in Appendix I and a list of current membership of the Finance Committee is set out in Appendix II.

1.2 The Code is principally an initiative of the private sector as indicated by the membership of JPK1. The need for a Code was inspired in part by a desire for the private sector to initiate and lead a review and to establish reforms of standards of corporate governance at a micro level. This is based on the belief that in some aspects, self-regulation is preferable and the standards developed by those involved may be more acceptable and thus more enduring.

1.3 The Code essentially aims to set out principles and best practices on structures and processes that companies may use in their operations towards achieving the optimal governance framework. These structures and processes exist at a micro-level which include issues such as the composition of the board, procedures for recruiting new directors, remuneration of directors, the use of board committees, their mandates and their activities.

1.4 The significance of the Code is that it allows for a more constructive and flexible response to raise standards in corporate governance as opposed to the more black and white response engendered by statute or regulation. It is in recognition of the fact that there are aspects of corporate governance where statutory regulation, is necessary and others where self-regulation, complemented by market regulation is more appropriate.

1.5 The impact the Code will have in raising standards of corporate governance can be seen from the experiences of other jurisdictions. To quote the Hampel Committee<sup>1</sup>,

“... it is generally accepted that implementation of the Code’s (Cadbury Code of Best Practices) provisions has led to higher standards of governance and greater awareness of their importance. ...it is clear that Greenbury’s primary aim - full disclosure - is being achieved.”

1.6 The Cadbury Committee published a report on compliance with the Code in May 1995. The report showed that significant changes had taken place in the structure of UK boards, in line with the committee’s recommendations.<sup>2</sup> Greater

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<sup>1</sup> Paragraph 1.8 and 1.9 Final report of the Hampel Committee on Corporate Governance

<sup>2</sup> What is hard to tell, however, is how far these structural changes were translated into changes in the working of the board. In other words, are these changes more of form than of substance?

awareness of corporate governance issues is a first step towards good corporate governance. The level of awareness and attention generated by the Cadbury report has been phenomenal. The report has struck a chord internationally, and it has provided a yardstick against which standards of corporate governance are being measured.

- 1.7 Of significance, is the aspirational and evolutionary way in which codes influence the expectations of society, that are eventually reflected in the law. The attention generated on corporate governance issues has already had an impact on evolving judicial interpretations of directors' duties. There is an increasing trend (internationally) to hold directors liable to a higher objective standard. The Australian case of *Daniels v Anderson*<sup>3</sup> which deals with the tortious duty of care owed by directors, is a clear instance of non-executive directors being increasingly held to an objective standard of care. The English case of *Dorchester Finance v Stebbings*<sup>4</sup>, is another such example.
- 1.8 The need for a code also results from economic forces and the need to re-invent the corporate enterprise, so as to efficiently meet emerging global competition. The world's economies are tending towards market orientation. In market-oriented economies, companies are less protected by traditional and prescriptive legal rules and regulations. Malaysia is no exception and the shift to a full-disclosure regime, to be completed by the year 2001 is such an example. Hence there is the need for companies to be more efficient and well-managed than ever before to meet existing and anticipated world-wide competition. The role of directors then increases in importance. The role of the board in hiring the right management, compensating, monitoring, replacing and planning the succession of senior management is crucial, as management undertakes the key responsibility for the enterprise's efficiency and competitiveness. The role of the Code is to guide boards by clarifying their responsibilities, and providing prescriptions strengthening the control exercised by boards over their companies.
- 1.9 In developing the Code we have been mindful of developments in other jurisdictions. We have endeavoured to keep the discussion at an international level. Standards developed for Malaysia must measure up to international thinking on this subject.

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<sup>3</sup> [1995] 37 NSWLR 438

<sup>4</sup> [1989] BCLL

## 2 The Approach Under the Malaysian Code on Corporate Governance

2.1 There are three broad approaches to the issue of corporate governance that have been undertaken by jurisdictions around the world -

- A prescriptive approach - where the standard of corporate governance is set by specifying desirable practices coupled with a requirement to disclose compliance with them. For example, the London Stock Exchange adopts a standard best practice benchmark for all listed companies.
- A non-prescriptive approach - This approach simply requires corporate governance practices in a company to be disclosed. The emphasis here is on the disclosure of actual corporate governance practices. The thinking behind this approach is that each company's corporate governance needs may be different and directors of companies should apply their minds to addressing these needs. The Australian Stock Exchange has taken this approach.
- The hybrid approach - This is the approach preferred by the Hampel committee. The Committee considered that there is a need for broad principles and that all concerned should then apply these flexibly and with common sense to the varying circumstances of individual companies. Good corporate governance is not just a matter of prescribing particular corporate structures and complying with a number of hard and fast rules. The need for principles surfaced from the review the Committee conducted of the Cadbury and Greenbury Codes, where the original intention of the committees has been largely ignored. To quote the Hampel report,

“Companies’ experience of the Cadbury and Greenbury codes has been rather different. Too often they believe that the codes have been treated as sets of prescriptive rules. The shareholders or their advisers would be interested only in whether the letter of the rule had been complied with - yes or no.”

2.2 In response to this, the Hampel report draws a distinction between principles of corporate governance and more detailed guidelines like the Cadbury and Greenbury Codes. To quote the Hampel report<sup>5</sup>,

“With guidelines, one asks, how far are they complied with? With principles, the right question is “How are they applied in practice?”

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<sup>5</sup> Paragraph 2.1

It was recommended that companies should include in the annual report a narrative statement of how they apply the relevant principles to their particular circumstances. Given that good corporate governance rests with the board of directors, the written description of the way in which the board has applied the principles of corporate governance represents a key part of the process. The Hampel committee therefore recommended that the current requirement for companies to confirm compliance with Cadbury prescriptions should be superseded by a requirement to make a statement to show how they (i) apply the principles, and (ii) comply with the combined code<sup>6</sup> and in the latter case, to justify any significant variances<sup>7</sup>.

- 2.3 The Committee considered the Hampel approach to be the most suited for the Malaysian context for two reasons; First, that best practice prescriptions are necessary. The work of the Committee has proceeded on the basis that standards of corporate governance in Malaysia are lacking and that there is a need to raise these standards. Therefore to go to the other extreme of merely requiring disclosure of existing corporate governance practices of Malaysian companies (such as that required by the Australian Stock Exchange in respect of its listed companies) is not sufficient. To take this route, one would have to be fairly comfortable with the standard of corporate governance practiced in public listed companies.
- 2.4 In this respect it is equally important that these prescriptions are accompanied by a rule requiring disclosure of the extent to which listed companies have complied with the prescriptions and where they have not, the reasons why. It is not proposed that companies should be required to comply strictly with the prescriptions developed. Each company should have the flexibility to develop its own approach to corporate governance. And while the prescriptions establish a sound approach to corporate governance, companies may develop alternatives that may be just as sound. Nevertheless the prescriptions set the standard that companies must measure up to. Such a rule also ensures that the investment community receives an explanation for the company's approach to governance so that it is in a position to support the approach or work to influence change.
- 2.5 Second, that companies must nevertheless be encouraged to consciously address their governance needs. This was the thrust of the Cadbury report. But as alluded to earlier, the experience in the UK suggests that too often companies comply with the strict letter of the best practice prescriptions without regard to the spirit of it.
- 2.6 The biggest problem with a prescriptive approach is that it would encourage directors to concentrate on form rather than on exercising their judgement on what corporate governance practices are best for their companies. Directors may then adopt a practice of ticking a series of boxes to indicate that they have

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<sup>6</sup> The Hampel Committee recommended and has now produced as set of principles and a Code of Good Corporate Governance practice, which will embrace the recommendations of Cadbury, Greenbury as well as the Hampel committee.

<sup>7</sup> The recommendations of the Hampel committee have been accepted by the London Stock Exchange



complied with the prescribed best practices. This can be seized on as an easier option rather than the diligent pursuit of corporate governance objectives. Additionally the checklist method of ticking every box may be perceived by investors as implying endorsement by the regulator<sup>8</sup> of the company's corporate governance practices. Shareholders or their advisers would be interested only in whether the letter of the rule has been complied with - yes or no. A "yes" would receive a tick.

2.7 Perhaps most worrying is the fact pointed out by the Hampel committee that under such a box ticking system, it would not be difficult for lazy or unscrupulous directors or shareholders, to arrange matters so that the letter of every governance rule is complied with but not the substance. It might even be possible for the next disaster to emerge in a company with, on paper, a 100% record of compliance. The true safeguard for good corporate governance lies in the application of informed and independent judgement by experienced and qualified individuals - executive and non-executive directors, shareholders and auditors. "Box ticking" is neither fair to companies, nor likely to be efficient in preventing abuse. We have the very real experience in Malaysia in the form of audit committees, where companies merely comply in form by setting up such committees without giving heed to the spirit of the requirement by ensuring, for example, the quality of the people within the committee.

2.8 The Hampel recommendations seek to address this issue by requiring companies to include in the annual report a narrative account of how they apply the broad principles set out in the code. They do not prescribe the form and content of the statements. Rather it aims to secure sufficient disclosure so that investors and others can assess the company's performance and governance practices, and can respond in an informed way.

### 3. The Recommendations

The recommendations set out in the Code are premised on a prescriptive approach to corporate governance. In this respect, the Code sets out four forms of recommendations:-

- **Principles**

Part 1 sets out broad principles of good corporate governance for Malaysia. The objective of principles is to allow companies to apply these flexibly and with common sense to the varying circumstances of individual companies. Companies will be required by the listing requirements of the KLSE to include in their annual report a narrative statement of how they apply the relevant principles to their particular circumstances. This is to secure sufficient disclosure so that investors and others can assess companies' performance and governance practices, and respond in an informed way.

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<sup>8</sup> In this case, the Exchanges

- **Best practices in corporate governance**  
Part 2 sets out best practices for companies. It identifies a set of guidelines or practices intended to assist companies in designing their approach to corporate governance. While compliance with best practices is voluntary, companies will be required as a provision of the listing requirements of the KLSE to state in their annual reports, the extent to which they have complied with the best practices set out in Part 2 and explain any circumstances justifying departure from such best practices.
- **Exhortations to other participants**  
Part 3 is not addressed to listed companies but to investors and auditors to enhance their role in corporate governance. These are purely voluntary.
- **Explanatory notes and “mere best practices”**  
Part 4 provides explanatory notes to the principles and best practices set out in Parts 1 and 2 and exhortations set out in Part 3. Additionally Part 4 also sets out best practices directed at listed companies that do not require companies to explain circumstances justifying departure from best practices - “mere best practices”.

## 4. Compliance

- 4.1 By virtue of paragraph 15.26 of the KLSE Listing Requirements, all listed companies should state in their annual report how they have applied the principles set out in Part 1 of the Code and the extent to which they have complied with the best practices set out in Part 2 and identify and give reasons for any areas of non-compliance, and where applicable, state the alternative practice(s) adopted.
- 4.2 In respect of Parts 1 and 2, boards are not expected to comment separately on each item of the Code with which they are complying, but areas of non-compliance will have to be dealt with individually.
- 4.3 It is recognised that smaller listed companies may initially have difficulty in complying with some aspects of the Code. The boards of smaller listed companies who cannot, for the time being comply with parts of the Code should note that they may instead give reasons for non-compliance.

### Sanctions for non-disclosure

- 4.4 Where a company fails to disclose the matters set out in para 4.1 in its annual report, it is open to the Exchange to take any action against the listed entity or its directors as set out in the listing requirements and section 11 of the Security Industry Act 1983.

# **THE MALAYSIAN CODE ON CORPORATE GOVERNANCE**

## **PART 1**

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### **PRINCIPLES OF CORPORATE GOVERNANCE**

# PART 1

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## PRINCIPLES OF CORPORATE GOVERNANCE

### A Directors

#### I The Board

Every listed company should be headed by an effective board which should lead and control the company.

#### II Board Balance

The board should include a balance of executive directors and non-executive directors (including independent non-executives) such that no individual or small group of individuals can dominate the board's decision making.

#### III Supply of Information

The board should be supplied in a timely fashion with information in a form and of a quality appropriate to enable it to discharge its duties.

#### IV Appointments to the Board

There should be a formal and transparent procedure for the appointment of new directors to the board.

#### V Re-election

All directors should be required to submit themselves for re-election at regular intervals and at least every three years.

### B Directors' Remuneration

#### I The Level and Make-up of Remuneration

Levels of remuneration should be sufficient to attract and retain the directors needed to run the company successfully. The component parts of remuneration should be structured so as to link rewards to corporate and individual performance, in the case of executive directors. In the case of non-executive directors, the level of remuneration should reflect the experience and level of responsibilities undertaken by the particular non-executive concerned.

#### II Procedure

Companies should establish a formal and transparent procedure for developing policy on executive remuneration and for fixing the remuneration packages of individual directors.

- III Disclosure  
The company's annual report should contain details of the remuneration of each director.

## C Shareholders

- I Dialogue between Companies and Investors  
Companies and institutional shareholders should each be ready, where practicable, to enter into a dialogue based on the mutual understanding of objectives.

- II The AGM  
Companies should use the AGM to communicate with private investors and encourage their participation.

## D Accountability and Audit

- I Financial Reporting  
The board should present a balanced and understandable assessment of the company's position and prospects.

- II Internal Control  
The board should maintain a sound system of internal control to safeguard shareholders' investment and the company's assets.

- III Relationship with the Auditors  
The board should establish formal and transparent arrangements for maintaining an appropriate relationship with the company's auditors.

## **PART 2**

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### **BEST PRACTICES IN CORPORATE GOVERNANCE**

### BEST PRACTICES IN CORPORATE GOVERNANCE

#### AA The Board of Directors

##### I Principal Responsibilities of the Board

The board should explicitly assume the following six specific responsibilities, which facilitate the discharge of the board's stewardship responsibilities -

- Reviewing and adopting a strategic plan for the company;
- Overseeing the conduct of the company's business to evaluate whether the business is being properly managed;
- Identifying principal risks and ensure the implementation of appropriate systems to manage these risks;
- Succession planning, including appointing, training, fixing the compensation of and where appropriate, replacing senior management;
- Developing and implementing an investor relations programme or shareholder communications policy for the company; and
- Reviewing the adequacy and the integrity of the company's internal control systems and management information systems, including systems for compliance with applicable laws, regulations, rules, directives and guidelines.

##### Constituting an effective board

##### II Chairman and Chief Executive Officer

There should be a clearly accepted division of responsibilities at the head of the company, which will ensure a balance of power and authority, such that no one individual has unfettered powers of decision. Where the roles are combined there should be a strong independent element on the board. A decision to combine the roles of Chairman and Chief Executive should be publicly explained.

##### III Board Balance

Non-executive directors should be persons of calibre, credibility and have the necessary skill and experience to bring an independent judgement to bear on the issues of strategy, performance and resources including key appointments and standards of conduct. To be effective, independent non-executive directors need to make up at least one third of the membership of the board.

## Size of non-executive participation

- IV In circumstances where a company has a significant shareholder, in addition to the requirement that one third of the board should comprise independent directors, the board should include a number of directors which fairly reflects the investment in the company by shareholders other than the significant shareholder. For this purpose, a “significant shareholder” is defined as a shareholder with the ability to exercise a majority of votes for the election of directors.
- V In circumstances, where the shareholder holds less than the majority but is still the largest shareholder, the board will have to exercise judgment in determining what is the appropriate number of directors which fairly reflects the investment in the company by the remaining holders of the shares.
- VI The board should disclose on an annual basis whether one third of the board is independent and in circumstances where the company has a significant shareholder, whether it satisfies the requirement to fairly reflect through board representation, the investment of the minority shareholders in a company. The board should disclose its analysis of the application of the best practices set out above, to the circumstances of the board.
- VII Whether or not the roles of Chairman and Chief Executive are combined, the board should identify a senior independent non-executive director of a board in the annual report to whom concerns may be conveyed.
- VIII **Appointments to the Board**  
The board of every company should appoint a committee of directors composed exclusively of non-executive directors, a majority of whom are independent, with the responsibility for proposing new nominees for the board and for assessing directors on an on-going basis. The actual decision as to who shall be nominated should be the responsibility of the full board after considering the recommendations of such a committee. The nominating committee should -
- Recommend to the board, candidates for all directorships to be filled by the shareholders or the board.
  - Consider, in making its recommendations, candidates for directorships proposed by the Chief Executive Officer and, within the bounds of practicability, by any other senior executive or any director or shareholder.
  - Recommend to the board, directors to fill the seats on board committees.
- IX The board, through the nominating committee, should annually review its required mix of skills and experience and other qualities, including core



competencies which non-executive directors should bring to the board. This should be disclosed in the annual report.

- X The board should implement a process, to be carried out by the nominating committee annually for assessing the effectiveness of the board as a whole, the committees of the board and for assessing the contribution of each individual director.
- XI Boards should be entitled to the services of a company secretary who must ensure that all appointments are properly made, that all necessary information is obtained from directors, both for the company's own records and for the purposes of meeting statutory obligations, as well as obligations arising from the Listing requirements of Exchanges or other regulatory requirements.
- XII **Size of Boards**  
Every board should examine its size, with a view to determining the impact of the number upon its effectiveness.
- XIII **Directors' Training**  
As an integral element of the process of appointing new directors, each company should provide an orientation and education program for new recruits to the board.

#### Board structures and procedures

- XIV The board should meet regularly, with due notice of issues to be discussed and should record its conclusions in discharging its duties and responsibilities. The board should disclose the number of board meetings held in a year and the details of attendance of each individual director in respect of meetings held.
- XV The board should have a formal schedule of matters specifically reserved to it for decision to ensure that the direction and control of the company is firmly in its hands.

#### Relationship of the board to management

- XVI The board, together with the Chief Executive Officer, should develop position descriptions for the board and for the Chief Executive Officer, involving definition of the limits to management's responsibilities. In addition, the board should approve, or develop with the Chief Executive Officer, the corporate objectives, which the Chief Executive Officer is responsible for meeting.
- XVII **Quality of Information**  
The board should receive information that is not just historical or bottom line and financial-oriented but information that goes beyond assessing the quantitative performance of the enterprise and looks at other performance factors such as

customer satisfaction, product and service quality, market share, market reaction, environmental performance and so on, when dealing with any item on the agenda.

- XVIII The chair of the board shall undertake primary responsibility for organising information necessary for the board to deal with the agenda and for providing this information to directors on a timely basis. If the chair is also the Chief Executive Officer, the board should also have in place a procedure to ensure that its agenda items are placed on the agenda and for providing this information to directors.
- XIX Access to Information  
Directors should have access to all information within a company whether as a full board or in their individual capacity, in furtherance of their duties.
- XX Access to Advice  
There should be an agreed procedure for directors, whether as a full board or in their individual capacity, in furtherance of their duties to take independent professional advice at the company's expense, if necessary.
- XXI All directors should have access to the advice and services of the company secretary.
- XXII Directors should appoint as secretary someone who is capable of carrying out the duties to which the post entails and their removal should be a matter for the board as a whole. The board should recognise that the Chairman is entitled to the strong and positive support of the company secretary in ensuring the effective functioning of the board.
- XXIII Use of Board Committees  
Where the board appoints a committee, it should spell out the authority of the committee, and in particular, whether the committee has the authority to act on behalf of the board or simply has the authority to examine a particular issue and report back to the board with a recommendation.
- XXIV Remuneration Committees  
Boards should appoint remuneration committees, consisting wholly or mainly of non-executive directors, to recommend to the board the remuneration of the executive directors in all its forms, drawing from outside advice as necessary. Executive directors should play no part in decisions on their own remuneration. Membership of the remuneration committee should appear in the directors' report.

The determination of remuneration packages of non-executive directors, including non-executive chairmen should be a matter for the board as a whole. The individuals concerned should abstain from discussion of their own remuneration.

## BB Accountability and Audit

### The audit committee

- I The board should establish an audit committee of at least three directors, a majority of whom are independent, with written terms of reference which deal clearly with its authority and duties. The Chairman of the audit committee should be an independent non-executive director.
- II The duties of the audit committee should include the following -
- (i) To consider the appointment of the external auditor, the audit fee and any questions of resignation or dismissal;
  - (ii) To discuss with the external auditor before the audit commences, the nature and scope of the audit, and ensure co-ordination where more than one audit firm is involved;
  - (iii) To review the quarterly and year-end financial statements of the company, focusing particularly on:-
    - Any changes in accounting policies and practices;
    - Significant adjustments arising from the audit;
    - The going concern assumption;
    - Compliance with accounting standards and other legal requirements;
  - (iv) To discuss problems and reservations arising from the interim and final audits, and any matter the auditor may wish to discuss (in the absence of management where necessary);
  - (v) To review the external auditor's management letter and management's response;
  - (vi) To do the following where an internal audit function exists:
    - review the adequacy of the scope, functions and resources of the internal audit function, and that it has the necessary authority to carry out its work;
    - review the internal audit programme and results of the internal audit process and where necessary ensure that appropriate actions are taken on the recommendations of the internal audit function;

- review any appraisal or assessment of the performance of members of the internal audit function;
  - approve any appointment or termination of senior staff members of the internal audit function;
  - inform itself of resignations of internal audit staff members and provide the resigning staff member an opportunity to submit his reasons for resigning.
- (vii) To consider any related party transactions that may arise within the company or group;
- (viii) To consider the major findings of internal investigations and management's response;
- (ix) To consider other topics as defined by the board.
- III The Finance director, the Head of Internal Audit (where such a function exists) and a representative of the external auditors shall normally attend meetings. Other board members may attend meetings upon the invitation of the audit committee. However, at least once a year the committee shall meet with the external auditors without executive board members present.
- IV The audit committee must have explicit authority to investigate any matter within its terms of reference, the resources which it needs to do so and full access to information. The committee should be able to obtain external professional advice and to invite outsiders with relevant experience to attend, if necessary.
- V The audit committee should meet regularly, with due notice of issues to be discussed and should record its conclusions in discharging its duties and responsibilities.
- VI The board should disclose in an informative way, details of the activities of audit committees, the number of audit meetings held in a year and details of attendance of each individual director in respect of meetings.
- VII The Board should establish an internal audit function. Where an internal audit function does not exist, the Board should assess whether there are other means of obtaining sufficient assurance of regular review and/or appraisal of the effectiveness of the system of internal controls within the company. The board should explain, in summary, the means that exist for obtaining such assurance of regular review and/or appraisal.

VIII The internal audit function should be independent of the activities they audit and should be performed with impartiality, proficiency and due professional care. The board or the audit committee should determine the remit of the internal audit function.

## CC Shareholders

### The relationship between the board and shareholders

I Boards must maintain an effective communications policy that enables both the board and management to communicate effectively with its shareholders, stakeholders and the public generally. This policy must effectively interpret the operations of the company to the shareholders and must accommodate feedback from shareholders, which should be factored into the company's business decisions.

## **PART 3**

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### **PRINCIPLES AND BEST PRACTICES FOR OTHER CORPORATE PARTICIPANTS**

## PART 3

### PRINCIPLES AND BEST PRACTICES FOR OTHER CORPORATE PARTICIPANTS

- I Shareholder Voting  
Institutional shareholders have a responsibility to make considered use of their votes.
- II Dialogue between Companies and Investors  
Institutional investors should encourage direct contact with companies including constructive communication with both senior management and board members about performance, corporate governance and other matters affecting shareholders' interest.
- III Evaluation of Governance Disclosures  
When evaluating companies' governance arrangements, particularly those relating to board structure and composition, institutional investors and their advisers should give due weight to all relevant factors drawn to their attention.
- IV External Auditors  
The external auditors should independently report to shareholders in accordance with statutory and professional requirements and independently assure the board on the discharge of its responsibilities under D.I and D.II above in accordance with professional guidance.

**PART 4**  
**EXPLANATORY NOTES**



### EXPLANATORY NOTES

#### PRINCIPLES OF CORPORATE GOVERNANCE

Directors are required by virtue of paragraph 15.26 KLSE Listing Requirements to include in their annual report a narrative statement of how they apply the principles set out in Part 1 to their particular circumstances. Given that the responsibility for good corporate governance rests with the board, a written description of the way in which the board applies the principles of good corporate governance, represents a key part of the process.

#### A The Board of Directors

##### I The Board

Every listed company should be headed by an effective board which should lead and control the company.

4.1 This endorses the unitary board structure for Malaysian companies. It stresses the dual role of the board - leadership and control - and the need to be effective in both. Within the context of a Malaysian board, this means a board made up of a combination of executive directors, who with their intimate knowledge of the business take on primary responsibility for leadership of the company and non-executive directors, who can bring a broader view to the company's activities, under a Chairman who accepts the duties and responsibilities that the post entails. A crucial pre-requisite to creating an effective board is the explicit assumption by the board of its principal responsibilities, which facilitate the discharge of the board's stewardship responsibilities.

##### II Board Balance

The board should include a balance of executive directors and non-executive directors (including independent non-executives) such that no individual or small group of individuals can dominate the board's decision making.

4.2 This highlights the need to avoid the board being dominated by one individual. It is important that there should be a sufficient number of independent directors who are not only independent but seen to be independent; and that these individuals should be able both to work co-operatively with their executive colleagues and to demonstrate objectivity and robust independence of judgement when necessary. The risk is perhaps greatest where the roles of Chairman and Chief Executive are combined. It is here that the presence of a sufficient number of independent directors is crucial.

##### III Supply of Information

The board should be supplied in a timely fashion with information in a form and of a quality appropriate to enable it to discharge its duties.

- 4.3 Information is power. The effectiveness of non-executive directors (indeed, of all directors) turns, to a considerable extent, on the quality of the information they receive. However individual directors do not have the time or the resources to obtain information from the company, relevant to the proposed board decision. There should be procedures in place to ensure that the board is supplied in a timely fashion with information.

#### IV Appointments to the Board

There should be a formal and transparent procedure for the appointment of new directors to the board.

- 4.4 The board's process for assessing existing directors and identifying, recruiting, nominating, appointing and orienting new directors is central to enhanced governance. This function can be performed by the board as a whole. But we endorse the view that the adoption of a formal procedure for appointments to the board, with a nomination committee making recommendations to the full board, should be recognised as good practice. This is dealt with in more detail in paragraphs 4.33 and 4.34 below.

#### V Re-election

All directors should be required to submit themselves for re-election at regular intervals and at least every three years.

- 4.5 We endorse the view that it is the board's responsibility to appoint new directors and the shareholders' responsibility to re-elect them. Re-election at regular intervals not only promotes effective boards but affords shareholders the opportunity to review the directors' performance in turn and where necessary, to replace them. This is consistent with Chapter 7 of the Listing Requirements which requires, among others, that a public listed company must have provisions in its articles of association for election of directors to take place every year.<sup>9</sup> The Listing Requirements go on to require all directors, including the managing director, to retire from office once at least in each three years, but shall be eligible for re-election.

## B Directors' Remuneration

- 4.6 Directors' remuneration should be embraced in the corporate governance process; the way in which directors' remuneration is handled can have a damaging effect on a company's public reputation, and on morale within the company. We suggest the following broad principles -

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<sup>9</sup> articles 63-66 Table A of Companies Act 1965 (CA) contain provisions relating to retirement by rotation.

I The Level and Make-up of Remuneration

Levels of remuneration should be sufficient to attract and retain the directors needed to run the company successfully. The component parts of remuneration should be structured so as to link rewards to corporate and individual performance, in the case of executive directors. In the case of non-executive directors, the level of remuneration should reflect the experience and level of responsibilities undertaken by the particular non-executive concerned.

- 4.7 This wording makes it clear that those responsible should consider the remuneration of each director individually, and should do so against the needs of the particular company for talent at board level at the particular time. The remuneration of executive directors should be linked to performance while the remuneration of non-executives should be linked to their experience and level of responsibilities undertaken.

II Procedure

Companies should establish a formal and transparent procedure for developing policy on executive remuneration and for fixing the remuneration packages of individual directors.

- 4.8 Whatever the procedure, directors, whether executive or non-executive, should not participate in decisions on their own remuneration packages.

III Disclosure

The company's annual report should contain details of the remuneration of each director.

- 4.9 Investor concern on remuneration practices in Malaysia is not at the level that it is in the United Kingdom, Australia and the United States. Nevertheless this disclosure requirement recognises and promotes important principles of fairness and accountability. Also, this principle implies that the report would be in the name of the board, rather than of the remuneration committee.

- 4.10 The company's annual report should therefore contain the details of remuneration of each director. Standards should be set which provide a rational and objective remuneration policy. For example, the objective of determining remuneration for a director might be to ensure that the company attracts and retains the directors needed to run the company successfully or linking remuneration rewards to corporate and individual performance.

## C Shareholders

### I Dialogue between Companies and Investors

Companies and institutional shareholders should each be ready, where practicable, to enter into a dialogue based on the mutual understanding of objectives.

4.11 This gives general endorsement to the idea of dialogue between companies and major investors.

### II The AGM

Companies should use the AGM to communicate with private investors and encourage their participation.

4.12 Private investors are able to make little contribution to corporate governance. The main way of achieving greater participation is through improved use of the AGM. We discuss a number of suggestions for this purpose in paragraph 4.79 below.

## D Accountability and Audit

### I Financial Reporting

The board should present a balanced and understandable assessment of the company's position and prospects.

4.13 This follows the Cadbury Code of Best Practices in the United Kingdom (UK). It is not limited to the statutory obligation to produce financial statements. The wording refers mainly to the annual report to shareholders, but the principle also covers interim and other price-sensitive public reports and reports to regulators.

### II Internal Control

The board should maintain a sound system of internal control to safeguard shareholders' investment and the company's assets.

4.14 This covers not only financial controls but operational and compliance controls, and risk management, since there are potential threats to shareholders' investments in each of these areas.

### III Relationship with the Auditors

The board should establish formal and transparent arrangements for maintaining an appropriate relationship with the company's auditors.

4.15 The duties of the audit committee required by the Listing Requirements should include keeping under review the scope and results of the audit and its cost effectiveness, and the independence and objectivity of the auditors.

## BEST PRACTICES IN CORPORATE GOVERNANCE

The enumerated text below (e.g. I,II, III) represents best practice benchmarks as set out in Part 2 of the Code. Part 2 is directed at directors of listed companies. While compliance with these guidelines is not mandated, companies are required by virtue of paragraph 15.26 KLSE Listing Requirements to make a statement in their annual report disclosing the extent of compliance with the best practices set out in Part 2. The statement shall include an explanation of circumstances justifying departure from the best practices and a description of the alternative practices adopted by the listed company, if any. Other best practice recommendations (“mere recommendations”) may be found in the text of the discussion below. Boards are not required to justify significant variances with “mere best practices” in the annual report. These are italicised and in bold for ease of reference.

### AA The Board of Directors

4.16 The key to good governance lies in getting the right board in place. A company with a properly balanced board and effective independent directors should be left to run its business, with the board being accountable for its stewardship. Our analysis of the role of the board involves a discussion of the responsibilities of the board, the constitution of the board and the structures and processes within the board.

4.17 Boards should assume responsibility over all of the principal responsibilities set out below to effectively lead and control the company.

#### I Principal Responsibilities of the Board

The board should explicitly assume the following six specific responsibilities, which facilitate the discharge of the board’s stewardship responsibilities.

- **Reviewing and adopting a strategic plan for the company**  
Modern organisational theory posits that defining a corporate goal or mission and defining the strategy to achieve it, are integral to corporate success. The leadership for this process comes from management. Management have the primary responsibility for articulating strategy because they have the greatest knowledge of the firm and its competitive environment and they ultimately execute the plan. The role of the board is clear in that they are to review, approve or disapprove management’s proposal. In doing so they should bring an objectivity and breadth of judgement to the strategic planning process as they are not involved in the day to day management of the business.

If the board is to independently judge the merits of a management's proposal concerning strategic or business plans, boards need to evaluate elements which should be taken into account in the process of creating the strategic plan for the company. These elements vary from company to company, but generically they include factors such as the existing and potential rivals of a company; the company's external environmental factors (economic, social and political); and the internal characteristics of an organisation (goals, assets, liabilities and structure).<sup>10</sup> The board should properly satisfy itself that management has taken into account all the appropriate elements.

The board is also responsible for monitoring management's success in implementing the strategy. In this respect it should identify and understand the benchmarks that will inform it of the plan's progress after implementation.

- **Overseeing the conduct of the company's business to evaluate whether the business is being properly managed**  
A basic function of the board is to oversee the performance of management to determine whether the business is being properly managed. The board's obligation to oversee the performance of senior management does not imply an antagonistic relationship between the board and the executives. Rather it contemplates a collegial relationship that is supportive yet watchful. In this respect the board must ensure that there are, objectives in place against which management's performance can be measured.
- **Identifying principal risks and ensure the implementation of appropriate systems to manage these risks**  
The board must understand the principal risks of all aspects of the business that the company is engaged in and recognising that business decisions require the incurrence of risk. The target is to achieve a proper balance between risks incurred and potential returns to shareholders. This requires boards to ensure that there are in place systems that effectively monitor and manage these risks with a view to the long term viability of the company.
- **Succession planning, including appointing, training, fixing the compensation of and where appropriate, replacing senior management**  
This reflects the fact that the board functions through delegation to management. The board must ensure management of the highest calibre in appointing, training, assessing and providing for succession. The key to the effective discharge of this job is to provide

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<sup>10</sup> Sharon Oster, *Modern Competitive Analysis* (2<sup>nd</sup> Ed., 1994)

for the best chief executive officer for the job as the chief executive officer is the company's business leader. The board will assess the chief executive officer's performance against the objectives established by the board in cooperation with the chief executive officer and will assess his or her contribution on corporate strategy. The board must also be satisfied that there are programmes in place to train and develop management and must also provide for the orderly succession of management.

- Developing and implementing an investor relations programme or shareholder communications policy for the company; and

The responsibility of the board here is to ensure that the company has in place a policy to enable the company to communicate effectively with its shareholders, other stakeholders and the public generally. The policy should ensure that it effectively interprets the operations of the company to the shareholders and must accommodate feedback from shareholders, which should be factored into a company's business decisions.

- Reviewing the adequacy and the integrity of the company's internal control systems and management information systems, including systems for compliance with applicable laws, regulations, rules, directives and guidelines.

This is a responsibility that firmly rests in the hands of the board. The results of the survey indicate that the majority of boards of Malaysian public-listed companies do not consider themselves ultimately responsible for ensuring that an effective system of internal control is in place. Boards have to ensure that there is a satisfactory framework of reporting on internal financial controls and regulatory compliance.

### Constituting an effective board

- 4.18 The composition of the board of directors of a listed company is one of the most crucial issues in corporate governance. Every public-listed company should be headed by an effective board which can both lead and control the business. Within the context of a unitary board system, this means a board made up of a combination of executive directors, with their intimate knowledge of the business, and of outside non-executive directors, who can bring a broader view to the company's activities, under a Chairman who accepts the duties and responsibilities that the post entails. The discussion here relates to the constitution of the board which is both capable of exercising independent judgement and which is perceived as capable of exercising independent judgement.

## II Chairman and Chief Executive Officer

There should be a clearly accepted division of responsibilities at the head of the company, which will ensure a balance of power and authority, such that no one individual has unfettered powers of decision. Where the roles are combined there should be a strong independent element on the board. A decision to combine the roles of Chairman and Chief Executive should be publicly explained.

4.19 There are two key tasks at the top of every public company - the running of the board and the executive responsibility for the running of the company's business. In respect of the running of the board, Chairmen are primarily responsible for the following:-

- the working of the board;
- the balance of membership, subject to board and shareholder approval;
- ensuring that all relevant issues are on the agenda;
- ensuring that all directors, executive and non-executive alike, are enabled and encouraged to play their full part in its activities. This includes making certain that directors, especially non-executive directors receive timely, relevant information tailored to their needs and that they are properly briefed on issues arising at board meetings; and
- ensuring that executive directors look beyond their executive function and accept their full share of responsibilities of governance.

The Chief Executive's task is to run the business and implement the policies and strategies adopted by the board.

4.20 The Chairman's role in securing good corporate governance is crucial. Given the importance and particular nature of the Chairman's role, it should in principle be separate from that of the Chief Executive. If the two roles are combined in one person, it represents a considerable concentration of power.

4.21 One issue that surfaces in the Malaysian context in respect of the role of the Chairman is the almost "too ready" acceptance of the views of the dominant voice at the meeting. There is a general unwillingness by boards to pursue debate and a perhaps an over - eager desire to find a consensual resolution to issues and problems. Achieving consensus more often than not is a compromise towards the most entrenched view on the board, of sometimes a single voice, rather than that of the majority of board members. The role of the independent Chairman becomes crucially important in two respects. First, he should encourage a healthy debate on the issue and bring to the board a healthy



level of scepticism and independence. Second, he should ensure that every board resolution is put to a vote to ensure that it is the will of the majority and not that of the dominant owner that prevails.

### III Board Balance

Non-executive directors should be persons of calibre, credibility and have the necessary skill and experience to bring an independent judgement to bear on the issues of strategy, performance and resources including key appointments and standards of conduct. To be effective, independent non-executive directors need to make up at least one third of the membership of the board.

- 4.22 The calibre of non-executive members of the board is of special importance in setting and maintaining standards of corporate governance. Non-executive directors are appointed onto boards for various reasons - to make positive contribution as equal board members to the development of the company's strategy; to tap on their skills and expertise derived from their diverse backgrounds<sup>11</sup>, to represent their interests on the board in the case of substantial shareholders and to provide a balanced and independent view onto the board. However, a special quality that non-executive directors, particularly independent non-executive directors, should bring to board deliberations is that of independence of judgement. Hence the requirement that independent non-executive directors need to make up at least one third of the membership of the board. This recognises that there may be non-executive directors who are not "independent" who may nonetheless make a useful contribution to the board.

#### Definition of the term "independent"

- 4.23 The term independent in the Malaysian context refers broadly to two crucial aspects - independence from management and independence from a significant shareholder. The concept of independence varies from country to country. The Cadbury definition of independence essentially focuses on independence from management. This reflects the shareholding structure of companies in the UK where it typically involves a separation of management and control. Therefore, efforts are generally directed towards strengthening controls over management. The Toronto Stock Exchange (TSE) Committee report on corporate governance on the other hand, requires two types of independent elements on the board. First, the concept of unrelated directors who are essentially directors independent of management. The second type of independent element that was considered necessary by the TSE Committee essentially relates to independence from a significant or controlling shareholder. The purpose of this constraint on the significant shareholder's ability to elect the board, is to ensure in general terms that there is a component of the board, at least in numbers, generally reflecting the investment of the public or the minority shareholder in the company, which is not related to either the significant shareholder or the company. The definition

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<sup>11</sup> Particularly in smaller companies where these skills may not be otherwise available to management.

of “independent director” under Chapter 1 of the KLSE Listing Requirements similarly refers to independence from management and independence from a “major shareholder”. The term “major shareholder” is defined in Chapter 1 of the Listing Requirements.

#### Size of non-executive participation

- 4.24 Even where an independent non-executive chooses to take a stand against management he is more often than not outvoted by the executive members of the board, or in cases where a significant shareholder controls the board, by the latter. The number of independent non-executives is significant and it should be such that their views will carry significant weight in board decisions.
- 4.25 There are divergent views internationally on the size and number of independent non-executive directors on the board. The Cadbury Committee suggested that there be at least three non-executive directors on the board of which a majority should be independent. The Hampel Committee on corporate governance was of the opinion that if non-executive directors are to be effective on the board, they should make up not less than one third of the board, again a majority of which should be independent. The Report of the TSE Committee on Corporate Governance in Canada, proposes as a Guideline that every board should be constituted with a majority of individuals who qualify as unrelated. The term “unrelated” essentially refers to independence from management.
- 4.26 The results of the KLSE/Pricewaterhouse Coopers survey<sup>12</sup> indicate that there is a reasonably proportionate mix of independent non-executive directors (average number - 2.6), non-executive directors (average number - 2.6) and executive directors (average number - 2.5). The average board size was found to be 8 persons. On average therefore independent non-executive directors constitute about one third of the board. This is the methodology by which the committee arrived at this prescription. The committee preferred this approach as opposed to that of prescribing a figure because the figure must correspond to the board size and in this respect the size of companies listed on the KLSE and, therefore, their board sizes vary significantly. The requirement that one third of the board must be independent takes into account the varying board sizes of these companies.

IV In circumstances where a company has a significant shareholder, in addition to the requirement that one third of the board should comprise independent directors, the board should include a number of directors which fairly reflects the investment in the company by shareholders other than the significant shareholder.<sup>13</sup> For this purpose, a “significant shareholder” is defined as a shareholder with the ability to exercise a majority of votes for the election of directors.

<sup>12</sup> The KLSE in conjunction with Price Waterhouse Coopers have conducted a survey of corporate governance towards understanding standards of corporate governance practised by Malaysian corporations - i.e - The KLSE/Price Waterhouse Coopers Joint Survey of Corporate Governance Practices in Public-Listed Companies 1998

<sup>13</sup> The committee essentially adopted the proposal of the TSE Committee on Corporate Governance in its Guidelines for Improved Corporate Governance in Malaysia - Where were the Directors? It should be noted that the Canadian corporate landscape is not unlike ours where there are a number of companies which have a significant shareholder - a shareholder whose holdings are such that it can exercise or influence the control of the company.

- 4.27 This recommendation introduces a form of proportional representation. For example, if the significant shareholder holds shares representing two thirds of the equity and two thirds of the votes for the election of the directors of the company which has a board of 9 directors and which wishes to satisfy this best practice, the holder can elect up to 6 directors who have interests in or relationships with the significant shareholder.
- 4.28 However this recommendation only extends to circumstances where the significant shareholder is also the majority shareholder, i.e. the shareholder able to exercise majority votes for the election of directors. It is not extended to cover situations where the significant shareholder holds less than the majority but is still the largest shareholder.
- V In circumstances, where the shareholder holds less than the majority but is still the largest shareholder, the board will have to exercise judgement in determining what is the appropriate number of directors which fairly reflects the investment in the company by the remaining holders of the shares.
- 4.29 If the proportional representation requirement is applied, the holder of one third of the shares of the company with a 9 director board could only elect three directors not related to the holder. Proportional representation in this respect may compromise the ability of the significant shareholder to exercise control and execute his or her strategy for the company. Also, practically speaking, the committee found it impossible to believe that independent directors, no matter how well compensated, spend anywhere near the amount of time thinking about the future of the company as would such a majority shareholder. In any case investors when acquiring shares in a company with a significant shareholder, are generally aware of the shareholding and rely in many cases on the significant shareholder to exercise control and execute his or her strategy for the company.
- 4.30 In these circumstances, the board will have to exercise its judgement in determining what is the appropriate number of directors, which fairly reflects the investment in the company by the remaining holders of the shares.
- VI The board should disclose on an annual basis whether one third of the board is independent and in circumstances where the company has a significant shareholder, whether it satisfies the requirement to fairly reflect through board representation, the investment of the minority shareholders in a company. The board should disclose its analysis of the application of the best practices set out above, to the circumstances of the board.

4.31 This leaves it to the market to judge the composition and effectiveness of the board. Investors must take a positive interest in the composition of boards of directors, with checks and balances, and to the appointment of a core of non-executive directors of the necessary calibre, experience and independence.

VII Whether or not the roles of Chairman and Chief Executive are combined, the board should identify a senior independent non-executive director of a board in the annual report to whom concerns may be conveyed.

4.32 This essentially adopts the recommendation by the Hampel Committee on Corporate Governance in the UK. This applies even where the roles of Chairman and Chief Executive are separate in recognition that every board needs vigorously independent non-executive directors. There can, in particular, be occasions, when there is a need to convey concerns to the board other than through the Chairman and Chief Executive. Such a situation could arise where an autocratic Chairman is closely allied to a powerful Chief Executive. Although in such a situation the roles of Chairman and Chief Executive were separated, there would be a need for a mechanism whereby directors could take a concern to an identified independent figure. The identification of such a non-executive is generally regarded as an essential “safety valve”. It is not envisaged that such an individual would for this purpose need special responsibilities or an independent leadership role.

VIII Appointments to the Board

The board of every company should appoint a committee of directors composed exclusively of non-executive directors, a majority of whom are independent, with the responsibility for proposing new nominees for the board and for assessing directors on an on-going basis. The actual decision as to who shall be nominated should be the responsibility of the full board after considering the recommendations of such a committee. The nominating committee should -

- Recommend to the board, candidates for all directorships to be filled by the shareholders or the board.
- Consider, in making its recommendations, candidates for directorships proposed by the Chief Executive Officer and, within the bounds of practicability, by any other senior executive or any director or shareholder.
- Recommend to the board, directors to fill the seats on board committees.

4.33 The board's process for assessing existing directors and identifying, nominating, appointing and orienting new directors is central to enhanced governance. This function can be performed by the board as a whole but as a matter of best practice we recommend that this responsibility be delegated to a committee. The nomination committee removes from the Chief Executive Officer, the general responsibility for constituting the board. A director who is beholden to the Chief Executive Officer will have difficulty in acting independently, at least in assessing management. The nominating committee should not have the delegated power from the board to implement its recommendations but should be obliged to report its recommendations back to the full board for its consideration and implementation. This is in recognition of the importance of chemistry within the board and the need for board membership to be endorsed by all or the majority. Boards of directors function most effectively if they are forthright and collegial, rather than secretive and confrontational, either in discussions between themselves or in their discussions with management.

IX The board, through the nominating committee, should annually review its required mix of skills and experience and other qualities, including core competencies which non-executive directors should bring to the board. This should be disclosed in the annual report.

4.34 The board should at least annually identify the mix of skills and experience and other qualities it requires for it to function completely and efficiently. It is of course possible for a board to access particular skills and experience either within the company or from external advisers. However, depending on the company's business it is likely that there will be certain skills and experience which are so strategic and fundamental to success that they should exist at the board level itself and in particular amongst the independent directors.

X The board should implement a process, to be carried out by the nominating committee annually for assessing the effectiveness of the board as a whole, the committees of the board and for assessing the contribution of each individual director.

4.35 Assessing the contribution of individual directors is not an assessment related to the performance of the company nor is it an assessment designed to relate director compensation to company performance. The assessment of directors is an examination of each individual director's ability to contribute to the effective decision making of the board. Each board will have its own approach to assessing its effectiveness and the contribution of members. In the latter respect companies should identify a criteria for individual contributions and should be willing to provide feedback to directors in respect of their individual performance. This process of assessment is necessary for it will make directors aware that their performance is being reviewed by their fellow directors and should enhance each director's contribution. The process may also provide constructive input to each individual director as to how he or she may better contribute to the functioning of the board.

XI Boards should be entitled to the services of a company secretary who must ensure that all appointments are properly made, that all necessary information is obtained from directors, both for the company's own records and for the purposes of meeting statutory obligations, as well as obligations arising from the Listing rules of Exchanges or other regulatory requirements.

4.36 It is crucial that company secretaries undertake the task of handling all of the preparatory work that has to be completed and information that has to be gathered prior to the directors taking up their posts. This includes ensuring that the appointments are correctly made and that all relevant information that the company requires from directors are obtained. The amount of information required from new directors is vast. It covers information that is required for the company's own records, that which is required to meet statutory obligations and information for Exchanges and the regulators. Failure to provide this information speedily may result in fines and late filing penalties being imposed on directors, the company or both and in some cases criminal liability on directors.

4.37 It is not just the company that requires information from its directors. If directors are to make a speedy and effective contribution, then they also require information. Company secretaries should be in a position to provide every new director with essential information that he will require to undertake his functions and such additional information as and when appropriate.

4.38 In this respect, the relevant professional organisations should develop a best practices guide to provide a useful checklist for the more experienced company secretary to ensure that appointments are properly made and provide checklists of all information required from and by a new director. This will also act as an invaluable guide for the less experienced company secretary.

## XII Size of Boards

Every board should examine its size, with a view to determining the impact of the number upon effectiveness.

4.39 The number of directors constituting a board is an important factor in determining the effectiveness of the board. The problem with boards that are too big is that the individual directors may feel constrained about actively participating in board decisions and hence have little sense of personal accountability. There also may be difficulty in individuals functioning within time constraints and their ability to make effective decisions. Some boards may also be too small. Bearing in mind the principal responsibilities of the board, each board should ensure that it has enough directors to discharge these responsibilities and perform those functions.

### XIII Directors' Training

As an integral element of the process of appointing new directors, each company should provide an orientation and education program for new recruits to the board.

- 4.40 The program could be a one or two day event which would involve educating the director as to the nature of the business, current issues within the company and the corporate strategy, the expectations of the company concerning input from directors, and the general responsibilities of directors. Some companies have developed orientation manuals. However, the manual is just a beginning. The program should include the opportunity to discuss with experts the responsibilities of a director and of the board as a whole as well as the opportunity to visit facilities and to meet with corporate officers to discuss and better understand the business which will allow the director to contribute effectively from the outset of the appointment.
- 4.41 It is equally important that directors should receive further training from time to time, particularly on relevant new laws and regulations and changing commercial risks.

### Number of directorships

- 4.42 The Committee concluded that it would not be practicable to prescribe a maximum number of directorships that a person should be entitled to hold. However, we recommend that the nominating committee in assessing the suitability of an individual to be elected to the board will take into account the individual's other commitments, resources and time available for input for the board.<sup>14</sup>

### Board structures and procedures

- 4.43 The effectiveness of a board is buttressed by its structures and procedures.

XIV The board should meet regularly, with due notice of issues to be discussed and should record its conclusions in discharging its duties and responsibilities. The board should disclose the number of board meetings held a year and the details of attendance of each individual director in respect of meetings held.

- 4.44 The KLSE/Price Waterhouse Coopers survey results indicate that over one third of companies, held three or less full board meetings a year, while 5% of companies surveyed only held one. The Committee considered that stipulating a minimum figure for board meetings to be unpracticable. However, it is difficult to imagine how a board is in control of the company if it meets less

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<sup>14</sup> The government has since taken a policy decision to restrict the number of directorships that may be held by directors of public listed companies. This restriction is implemented through the Listing Requirements of the KLSE.

than four times. We recommend instead that the directors should be required to disclose the number of board meetings held a year and the details of the attendance of each individual director to enable shareholders to evaluate the commitment of a particular director to the affairs of the company. It is then for the shareholder to satisfy himself whether the board is in control of the company.

XV The board should have a formal schedule of matters specifically reserved to it for decision to ensure that the direction and control of the company is firmly in its hands.

4.45 This acts as a safeguard against misjudgements and possible illegal practices. A schedule of matters should be given to directors on appointment and should be kept up to date. Such a schedule would at least include:-

- Acquisitions and disposal of assets of the company or its subsidiaries that are material to the company;
- Investments in capital projects, authority levels, treasury policies and risk management policies.

Boards should lay down rules to determine materiality for any transaction and should establish clearly which transactions require multiple board signatures. Boards should also agree on the procedures to be followed when exceptionally, decisions are required between board meetings.

#### Relationship of the board to management

4.46 Many of the responsibilities of the board are delegated by the board to management. A key principle to the effective functioning of the board is that it is able to function independently of management. There should be an adequate degree of independence and a process or practice in place to allow directors to meet and actively exchange views. In the absence of this ability, a board cannot effectively assess the direction of the company and the performance of management - one of the board's principal responsibilities.

4.47 The chair or the committee or other director assigned this responsibility, is responsible for managing the processes of the board and for ensuring that the board discharges the responsibilities we have previously defined for it. Appropriate procedures may involve the board meeting on a regular basis without management present or may involve expressly assigning the responsibility for administering the board's relationship to management to a committee of the board.

XVI The board, together with the Chief Executive Officer, should develop position descriptions for the board and for the Chief Executive Officer, involving definition of the limits to management's responsibilities. In



addition, the board should approve, or develop with the Chief Executive Officer, the corporate objectives, which the Chief Executive Officer is responsible for meeting.

- 4.48 It is important for the board and management to undertake this exercise. The allocation should reflect the dynamic nature of the relationship necessary for the company to adapt to changing circumstances. There will be no one correct prescription for the allocation of responsibilities; it will depend on the circumstances of every company. The allocation of responsibility can be expressed by defining the limits to management's authority on the assumption that corporate action beyond this authority is the responsibility of the board. Position descriptions should also be prepared for the chair of the board.

XVII Quality of Information

The board should receive information that is not just historical or bottom line and financial oriented but information that goes beyond assessing the quantitative performance of the enterprise and looks at other performance factors such as customer satisfaction, product and service quality, market share, market reaction, environmental performance and so on, when dealing with any item on the agenda.

- 4.49 This is a point stressed by the TSE Committee on corporate governance. We wish to underscore the importance of the board receiving information that is not just historical or bottom line and financial oriented. An effective board of directors will seek information that goes beyond assessing the quantitative performance of the enterprise and looks at other performance factors such as customer satisfaction, product and service quality, market share, market reaction, environmental performance and so on.

XVIII The chair of the board shall undertake primary responsibility for organising information necessary for the board to deal with the agenda and for providing this information to directors on a timely basis. If the chair is also the Chief Executive Officer, the board should also have in place a procedure to ensure that its agenda items are placed on the agenda and for providing this information to directors.

- 4.50 All boards should specifically allocate the responsibility for setting the board agenda and for organising and circulating the information relevant to the agenda on a timely basis.

XIX Access to Information

Directors should have access to all information within a company whether as a full board or in their individual capacity, in furtherance of their duties.

4.51 We endorse the view of the Cadbury report, when they say that the effectiveness of non-executive directors turns to a considerable extent on the quality of information that they receive and the use they make of it. All directors (executive and non-executive), have the same right of access to information. Non-executive directors lack the inside knowledge of the company of the executive directors, but they have the same right to information as they do. The company should ensure that they are granted this access.

XX Access to Advice

There should be an agreed procedure for directors, whether as a full board or in their individual capacities, in furtherance of their duties to take independent professional advice at the company's expense, if necessary.

4.52 Occasions may arise when directors have to seek legal or financial advice in the furtherance of their duties. They should always be able to consult the company's advisers. If however they consider it necessary to take independent professional advice, it is recommended that they should be entitled to do so at the company's expense, through an agreed procedure laid down formally. To impose some discipline upon the engagement of outside experts, we recommend that the engagement by an individual director of an outside expert be subject to the approval of the appropriate committee of the board.

XXI All directors should have access to the advice and services of the company secretary.

4.53 The company secretary has a key role to play in ensuring that board procedures are followed regularly and are reviewed. It should be standard practice for company secretaries to administer, attend and prepare minutes of board proceedings. The proximity that a company secretary has to the board of directors also makes them the perfect candidate for undertaking an advisory role in relation to the board in respect of compliance issues. This then follows through into a crucial role in encouraging compliance with the law.

4.54 The Chairman will look to the company secretary for guidance to the board on what their responsibilities are under the rules and regulations to which they are subject and how those responsibilities should be discharged. The compliance advice should extend to embrace all laws and regulations and not merely the routine filing requirements and other administrative requirements of the CA. The Cadbury Committee considered it the role of the company secretary to advise the chairman and the board on the implementation of the Code of Best Practice. Company secretaries in Malaysia should similarly equip themselves sufficiently to be able to render advice on matters pertaining to implementation of the Code.

XXII Directors should appoint as secretary someone who is capable of carrying out the duties to which the post entails and their removal should be a matter for the board as a whole. The board should recognise that the Chairman is entitled to the strong and positive support of the company secretary in ensuring the effective functioning of the board.

4.55 The responsibility for ensuring that the secretary remains capable and any questions as to the secretary's removal should be a matter for the board as a whole.

XXIII Use of Board Committees

Where the board appoints a committee, it should spell out the authority of the committee, and in particular, whether the committee has the authority to act on behalf of the board or simply has the authority to examine a particular issue and report back to the board with a recommendation.

4.56 In addition to the audit committee, which is required to be established by the listing rules of the Exchange, typical issues to be delegated to committees of larger public companies will include:

- Nominating directors, assessing the effectiveness of the board and the contribution of individual directors - this is alluded to earlier.
- Compensation and remuneration of directors and senior management.
- Internal controls and the integrity of the external audit.

4.57 The number of board committees will be a function of the size of the company and the board. Smaller companies will have fewer committees with some of them having responsibility for more than one area of the company's activities.

4.58 Sometimes boards delegate important powers to an executive committee. Where the executive committee approves important corporate plans and actions on an ongoing basis, the composition of such an executive committee should approximate the composition of the full board. There should be enough independent elements to approximate the proportion of such directors on the full board.

## B Directors' Remuneration

4.59 Board remuneration is an important aspect of effective corporate governance. The remuneration of directors should be appreciable and should reflect the responsibility and commitment which goes with board membership. This applies

to both executive as well as non-executive directors. If directors are paid a token amount there may be a tendency to think that the job is not important. On the other hand, if remuneration is excessive, the director may lose his or her independence. He or she will be perceived as someone who cannot afford to put his or her director's position on the line.

#### XXIV Remuneration Committees

Boards should appoint remuneration committees, consisting wholly or mainly of non-executive directors, to recommend to the board the remuneration of the executive directors in all its forms, drawing from outside advice as necessary. Executive directors should play no part in decisions on their own remuneration. Membership of the remuneration committee should appear in the directors' report.

The determination of remuneration packages of non-executive directors, including non-executive chairmen should be a matter for the board as a whole. The individuals concerned should abstain from discussion of their own remuneration.

## BB Accountability and Audit

### The audit committee

An independent audit committee serves to implement and support the oversight function of the board in several ways.

- Such a committee provides a means for review of the company's processes for producing financial data, its internal controls, and the independence of the company's external auditor, and a forum for dialogue with the company's external and internal auditors. In theory, the full board might execute these functions itself, because the board is obliged in any event to be conversant with those matters. In practice, however, there are several reasons why an audit committee would normally constitute a preferable location for these functions. For one thing, a focused review and detailed discussion of the company's processes for producing financial data, its internal controls, and independence of its external auditor might be too time-consuming for the full board. For another, because the company's financial data concerns the performance of management, it is important to have a forum for discussing this data, and the manner of its preparation, in which management participates only on request.
- An independent audit committee reinforces the independence of the company's external auditor, and thereby helps assure that the auditor will

have free rein in the audit process. This reinforcement is achieved in part by conferring, on an organ that is independent of the management whose financial results are being audited, a vital role in the retention, discharge, and compensation of the external auditor.

- An independent audit committee provides a forum for regular, informal, and private discussion between the external auditor and directors who have no significant relationships with management. In the absence of such a forum, an external auditor would often be reluctant to call for a meeting at the board level unless a problem of great magnitude had arisen. In contrast, the provision of an institutionalised forum facilitates and indeed encourages the external auditor to raise potentially troublesome issues at a relatively early stage, allows the auditor to broach sensitive problems in an uninhibited and private fashion, and gives the auditor assurance that it can readily get a hearing in the event of disagreement with management.
- An independent audit committee reinforces the objectivity of the internal auditing department (if there is one). If that department reports primarily to management (as is normally the case), and has no regular access to the board or to a board committee, it may encounter resistance to recommendations that do not meet with management's approval. Regular access to an audit committee may help ameliorate such resistance. A working relationship with an audit committee is also likely to increase the status and therefore the effectiveness of the internal auditing department.

4.60 The requirement for audit committees are set out in the Listing Requirements which require all listed companies to have audit committees comprising 3 members of whom a majority shall be independent. The Listing Requirements also set out the minimum functions of the audit committee. The objective of the Code is to flesh out the specific duties of the audit committee within the general functions set out in the rules.

I The board should establish an audit committee of at least three directors, a majority of whom are independent, with written terms of reference which deal clearly with its authority and duties. The Chairman of the audit committee should be an independent non-executive director.

4.61 This essentially sets out the existing requirement under the Listing Requirements. The appointment of a properly constituted audit committee is an important step in raising standards of corporate governance. Their effectiveness depends on their having a strong chairman who has the confidence of the board, the auditors and on the quality of the independent directors. Membership of the audit committee is a demanding task requiring commitment, training and skill. The directors concerned need to have a sufficient understanding of the issues to be dealt with by the committee to take an active part in its proceedings.

4.62 One issue that the Committee was asked to deal with is the issue relating to the presence of controlling shareholders and substantial shareholders, who are also the non-executive directors of a company, on the audit committee. These persons would have a vested interest in ensuring that the financial affairs of the company are properly handled. It is a powerful monitoring tool in ensuring that the interests of management are at all times aligned with that of the owners. In this respect, we recommend that such persons should be encouraged to participate in audit committees, subject to the requirement that the majority of the directors should, nevertheless, remain independent as defined by the Listing Requirements.

II The duties of the audit committee should include the following -

- (i) To consider the appointment of the external auditor, the audit fee and any questions of resignation or dismissal;
- (ii) To discuss with the external auditor before the audit commences, the nature and scope of the audit, and ensure co-ordination where more than one audit firm is involved;
- (iii) To review the quarterly and year-end financial statements of the company, focusing particularly on:-
  - Any changes in accounting policies and practices;
  - Significant adjustments arising from the audit;
  - The going concern assumption;
  - Compliance with accounting standards and other legal requirements.
- (iv) To discuss problems and reservations arising from the interim and final audits, and any matter the auditor may wish to discuss (in the absence of management where necessary);
- (v) To review the external auditor's management letter and management's response;
- (vi) To do the following where an internal audit function exists:
  - review the adequacy of the scope, functions and resources of the internal audit function, and that it has the necessary authority to carry out its work;

- review the internal audit programme and results of the internal audit process and where necessary ensure that appropriate action is taken on the recommendations of the internal audit function;
- review any appraisal or assessment of the performance of members of the internal audit function;
- approve any appointment or termination of senior staff members of the internal audit function;
- inform itself of resignations of internal audit staff members and provide the resigning staff member an opportunity to submit his reasons for resigning.

(vii) To consider any related party transactions that may arise within the company or group;

(viii) To consider the major findings of internal investigations and management's response;

(ix) To consider other topics as defined by the board.

III The Finance director, the Head of Internal Audit (where such a function exists) and a representative of the external auditors shall normally attend meetings. Other board members may attend meetings upon the invitation of the audit committee. However, at least once a year the committee shall meet with the external auditors without executive board members present.

IV The audit committee must have explicit authority to investigate any matter within its terms of reference, the resources which it needs to do so and full access to information. The committee should be able to obtain external professional advice and to invite outsiders with relevant experience to attend, if necessary.

V The audit committee should meet regularly, with due notice of issues to be discussed and should record its conclusions in discharging its duties and responsibilities.

4.63 PRO NED, United Kingdom's Guidelines for Audit, Committees are particularly useful on the issue of timing of audit committee meetings. It is essential to time meetings and plan agendas so that issues which have an impact on the company's prepared figures and published statements are discussed early enough to allow changes to be considered. The number of meetings required in a year depends

on the company's terms of reference and the extent of the complexity of the company's financial operations. What is usually required is the three or four meetings planned to coincide with the audit cycle and the timing of the published financial statements. Additionally, there may be ad hoc meetings in response to special circumstances as the company's affairs demand.

4.64 The PRO NED Guidelines state that the main meetings are often planned as follows:-

- Between the end of one year's audit and the beginning of the next  
Where the committee's remit extends to internal accounting systems as well as the audit process, a meeting early in the company's financial year is necessary to discuss the content of the management letter in the presence of the auditors, the approach to the current year's audit and any significant problems that can be foreseen, either as a result of the past year's experience or because of new accounting standards or other changes in statutory or listing requirements. Any discussion with the Finance Director as to the cost effectiveness of the audit should also take place at this stage.
- Before the issue of the Interim Statements  
In companies where the audit committee is responsible for reviewing these, this meeting will take place at an appropriate point before their release.
- After the Interim Results  
This may be a convenient point to review the company's systems of internal control in light of the interim report, and possibly also to discuss major reports prepared by the internal audit department.
- After the year end, but before the accounts are finalised  
This review of the annual financial statements should be timed so that checks and adjustments recommended as a result of the meeting can be carried out before the board meeting at which the accounts are adopted.

VI The board should disclose in an informative way, details of the activities of audit committees, the number of audit meetings held a year and details of attendance of each individual director in respect of meetings.

4.65 Currently, companies generally disclose the identities of their audit committee members and essentially set out the terms of reference of the company. Directors should be required to disclose the number of audit committee meetings held a year and the details of the attendance of each individual director to enable shareholders to evaluate the commitment of a particular director.



- 4.66 Preparation for membership of the audit committee  
Where a new member is appointed to the audit committee, the process for inducting a director, set out in XIII above should be supplemented, in consultation with the Finance director, by meetings with other members of management below board level responsible for the financial control system and those responsible for internal audit where there is one. Knowledge of the people concerned is as valuable as knowledge of the systems they operate.

### Internal audit

- VII The Board should establish an internal audit function. Where an internal audit function does not exist, the Board should assess whether there are other means of obtaining sufficient assurance of regular review and/or appraisal of the effectiveness of the system of internal controls within the company. The board should explain, in summary, the means that exist for obtaining such assurance of regular review and/or appraisal.
- 4.67 The internal audit function is an integral part of an effective system of corporate governance. References to an internal audit function include circumstances where a third party is contracted to perform the work concerned.
- VIII The internal audit function should be independent of the activities they audit and should be performed with impartiality, proficiency and due professional care. The board or the audit committee should determine the remit of the internal audit function.
- 4.68 The remit of the internal audit function should encompass the main role of the internal audit function that is to evaluate risk and monitor the effectiveness of the system of internal control. An independent and adequately resourced internal audit function should be in a position to assist the board in obtaining the assurance it requires regarding the effectiveness of the system of internal control. In addition, the Board or the audit committee should determine the general direction or remit of the internal audit function. The remit should be consistent with standards developed by the internal audit profession.

## CC Shareholders

### The relationship between the board and shareholders

- 4.69 The intimacy of the relationship between the board and management generally does not exist between the board and shareholders even though the directors are elected by and are accountable to the shareholders. The important exception is the significant shareholder that sits on the board or controls the board through his nominees.

## Interests represented by the board

- 4.70 This area is fraught with difficulties and appears to be an area of some confusion. In some ways, the presence of a controlling interest on a board is a check in that in such cases the controlling owners can provide the oversight over management that an independent board should provide in the absence of a controlling owner. However, in recognition of the fact that non-controlling shareholders need special vigilance at board level it has been recommended that the definition of independence should include independence from such controlling interest and the fact that the board should ensure that its composition reflects the ownership structure of the company. Beyond this the Committee finds it very difficult to control the activities of these persons through best practices.
- 4.71 The Committee nevertheless sought to clarify the confusion that exists in terms of the interests represented by the board.
- 4.72 As alluded to earlier, the expression of interests which must be reflected in board decisions is often extended from the interests of the company to the interests of the shareholders generally, on the theory that the ultimate responsibility for the board is to create value for shareholders and therefore what is in the best interests of the company should also be in the best interest of the owners.
- 4.73 We wish to emphasise that if the extension is made from the company to shareholders' generally, the board cannot use this definition to define its obligations in terms of the best interest of any single shareholder or any shareholder group. Perhaps most worrying is the fact that there are some directors who erroneously believe that if a particular shareholder is responsible for their election, the director should represent the best interest of that shareholder in his or her corporate decision making. It is not unheard of for some directors to reflect the best interest of a significant shareholder rather than the best interest of the company in a corporate decision. Directors must be scrupulous in identifying what they regard as the best interest of the company or its shareholders generally.
- 4.74 The problem is particularly acute in the case of nominee directors. A person who has a major stake in a company will often appoint some one that he trusts to the board in order to keep an eye on his investment. The nominee's relationship with his principal is a fiduciary one.<sup>15</sup> There is an issue therefore with regard to the competing fiduciary responsibilities of these persons. However, it must be highlighted that it is fairly well settled under law that a crucial aspect of the duties of nominee directors is that he is not entitled to sacrifice the interests of the company in favour of that of his principal. In this respect, Winslow J's dicta in *Raffles Hotel Ltd. v Rayner*<sup>16</sup> is instructive.

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<sup>15</sup> Re Syed Ahmad Alsagogg [1960] MLJ 147, where Tan Ah Tah J decided that a nominee director is a "trustee" for his principal.

<sup>16</sup> [1965] 1 MLJ 60

“A company is entitled to the undivided loyalty of its directors. A director who is the nominee of someone else should be left free to exercise his best judgement in the interests of the company he serves and not in accordance with the directions of his patron.”

- 4.75 It is accepted however that this rule is difficult in practice, as nominees are usually employees of the principal. Where the nominee is a non-executive director of a company, the position is less complex. The nominee can and should quite easily avoid conflicts of interest by simply refraining from participating in a decision where the interests of his principal and the company conflict.
- 4.76 But where the nominee is also an executive director, where he actually runs the business of the company, the instances of conflict are numerous and he may find it difficult to refrain from participating in a decision where the interests of his principal and the company conflict. There may also be greater pressure exerted on him to act in favour of his principal. In this regard, it is recommended that there must be strong independent elements on the board to provide such a check against the conduct of preferring the interests of the principal to the interests of the company.
- 4.77 Apart from this circumstance, the allocation of decision-making authority between the board and shareholders is generally not an issue. Decisions made by shareholders relate to the election of directors, the election of auditors, and generally to fundamental changes to the company’s constitution or business. Good governance also requires shareholder votes in circumstances where the board of directors may be interested in the transaction. This role, expressed through the voting power of ordinary shareholders, means that it is important for boards to maintain an active and constructive shareholders’ communications policy both through following the minimum requirements of the CA and voluntarily maintaining principles of good practice in handling shareholders’ affairs.
- I Boards must maintain an effective communications policy that enables both the board and management to communicate effectively with its shareholders, stakeholders and the public generally. This policy must effectively interpret the operations of the company to the shareholders and must accommodate feedback from shareholders, which should be factored into the company’s business decisions.
- 4.78 We encourage this relationship provided that information which a company provides to an investor should not qualify as undisclosed material information about the corporation.

## The AGM

4.79 The AGM is a crucial mechanism in shareholder communication. The AGM gives all shareholders, whatever the size of shareholding, direct public access to their boards. The question is how to enhance the format for AGMs so investors see the value in attending it. We believe that the AGM can be made a more meaningful and interesting occasion for all participants. To enhance the value of general meetings, our main recommendation is that there should be a specific effort to develop best practices in general meetings not unlike the best practices guide prepared by the Institute of Chartered Secretaries in the UK. Some recommendations in the context of improving the quality of AGMs are the following:-

- i. Boards should ensure that each item of special business included in the notice must be accompanied by a full explanation of the effects of a proposed resolution.
- ii. In the case of re-election of directors, boards should ensure that the notice of meetings state which directors are standing for election or re-election with a brief description to include matters such as age, relevant experience, list of directorships, date of appointment to the board, details of participation in board committees and the fact that a particular director is independent.
- iii. The Chairman should provide a reasonable time for discussion at the meeting. The Chairman should not attempt to limit discussion of genuine questions and the practice of discouraging shareholders from asking questions or being dismissive of questions is discouraged. Where appropriate, the Chairman should also undertake to provide the questioner with a written answer to any significant question which cannot be answered on the spot. He should exercise his discretion wisely in entertaining questions from shareholders. The Chairman's role in sifting the genuine questions from vexatious ones is crucial. Again a best practices guide to guide the Chairman in discharging this role is invaluable.
- iv. In companies whose AGMs are well-attended, companies, boards and/or management should conduct a business presentation with a question and answer session.
- v. Companies should count all proxies lodged with them in advance of the meeting, and without a poll being demanded,

resolution once it has been dealt with by the meeting on a show of hands. This will indicate publicly the proportion of total votes in respect of which proxies were lodged and the weight of shareholders' opinion revealed by those proxy votes. Publication could potentially see an increase in proxy votes.

- vi. Companies should provide shareholders upon request, with a summary of the discussion at the AGM. The Cadbury Committee recommended<sup>17</sup> that companies should after the event, send shareholders a brief summary of points raised at the AGM. The cost of doing this, either by a separate mailing or with the next financial report circulated to shareholders will be borne by the companies. However it must be borne in mind that the costs could be substantial, not least because of the printing costs involved. This is especially so in the case of companies with very large registers. The Hampel committee suggested instead that companies should prepare a resume of discussion at the meeting (but not a full detailed record), together with the voting figures on any poll or a proxy count where no poll was called and send this on the shareholder's request. The Committee recommends that companies should prepare a resume of discussion to be sent to shareholders upon request as a matter of best practice. This differs from the minutes of general meeting<sup>18</sup> as these normally record the conclusions and not the discussions.

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<sup>17</sup> Para 6.8

<sup>18</sup> which is a statutory requirement under section 156(1) Companies Act.

## PRINCIPLES AND BEST PRACTICES FOR OTHER CORPORATE PARTICIPANTS

These are not addressed to listed companies but are addressed to investors and auditors in recognition of the crucial role they play in corporate governance.

- I Shareholder Voting  
Institutional shareholders have a responsibility to make considered use of their votes.

4.80 Institutional shareholders include insurance companies, pension funds and professional fund managers. An important degree of common interest between a private investor and institutional investors is that they largely hold shares on behalf of individuals. In particular they have the same stake in standards of financial reporting and of governance in companies in which they have invested. Given the weight of their votes, the way in which institutional shareholders use their power to influence the standards of corporate governance is of fundamental importance. The wording above does not make voting mandatory; i.e. abstention remains an option; but these shareholders should, as a matter of good practice, make considered use of their votes. In this respect, institutional shareholders should take a positive interest in the composition of boards, with checks and balances, and to the appointment of a core of non-executives of necessary calibre, experience and independence. In this respect, local institutional shareholder associations should formulate guidelines for the development of a constructive relationship between the company and the owner.

- II Dialogue between Companies and Investors  
Institutional investors should encourage direct contact with companies including constructive communication with both senior management and board members about performance, corporate governance and other matters affecting shareholders' interest.

4.81 Shareholders receive reports and accounts and other explanatory circulars from companies which are required by statute or, for example by, the stock exchange. They also have the right to attend company meetings where they can raise questions about the affairs of a company. In addition some companies have a practice of making presentations to institutional or other shareholders. While these communications are necessary, they may not be sufficient to allow companies and shareholders to gain a full understanding of each others aims and requirements.

4.82 A direct dialogue gives investors a better appreciation of a company's objectives, its potential problems and the quality of its management, while also making a

company aware of the expectations and concerns of the shareholder. Two way communication between companies and institutions is an important aspect of corporate governance because corporate managers need full information about the assessments of institutions that hold their shares. Two way communication such as this helps create a more stable shareholder base. The belief is that shareholders will be willing to maintain their shareholding and take a longer term view of their investment if they have a better understanding of the corporate strategy.

4.83 We therefore encourage this relationship provided two issues are properly addressed.

- The information which a company provides to an investor should not qualify as undisclosed material information about the corporation.
- Companies should endeavour to ensure that the same opportunity should be available to all shareholders.

4.84 In this respect the best practice above clarifies that neither side should be required to enter into dialogue. Individual companies and investors must remain free to abstain from dialogue; the sheer numbers on both sides may make comprehensive coverage difficult.

### III Evaluation of Governance Disclosures

When evaluating companies' governance arrangements, particularly those relating to board structure and composition, institutional investors and their advisers should give due weight to all relevant factors drawn to their attention.

4.85 This stresses on the importance of considering disclosures on their individual merits, as opposed to 'box ticking'. Shareholders should show flexibility in the interpretation of the Code and should listen to directors' explanations and judge them on their merits.

### IV External Auditors

The external auditors should independently report to shareholders in accordance with statutory and professional requirements and independently assure the board on the discharge of their responsibilities under D.I and D.II under Part 1 of this Code in accordance with professional guidance.

4.86 This points up the dual responsibility of the auditors - the public report to shareholders on the statutory financial statements and on other matters as required by the Listing requirements; and additional private reporting to directors on operational and other matters.

## **APPENDICES**

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### **JPK WORKING GROUP 1**

### **MEMBERSHIP OF THE COMMITTEE**



## APPENDIX 1

### JPK WORKING GROUP 1 ON CORPORATE GOVERNANCE

Y Bhg Dato' Megat Najmuddin Khas  
Chairman, Federation of Public-Listed Companies Bhd - Chairman

Y Bhg Tan Sri Wan Azmi bin Wan Hamzah  
Chairman, Financial Reporting Foundation

Y Bhg Dato' Kok Wee Kiat  
President, Business Council For Sustainable Development Malaysia

Y Bhg Dato' J.J. Raj (Jr)  
Director General, Malaysian Institute of Directors

Dr Nordin Mohd Zain  
Board Member, Malaysian Accounting Standards Board

Puan Al-Baishah Hj Abdul Maran  
Deputy Registrar of Companies

Mr Khoo Beng Chit  
Senior Assistant Registrar of Companies

Ms Wong Sau Ngan  
Specialist (Legal & Regulatory Policy) Securities Commission

Ms Shanthi Kandiah  
Senior Executive, Securities Commission

Encik Izlan Izhah  
Executive Vice-President, Kuala Lumpur Stock Exchange

Cik Latifah Hj Yusof  
Senior Vice President, Listing, Kuala Lumpur Stock Exchange

Ms Qua Gek Kim  
Senior Vice President, Research & Publications, Kuala Lumpur Stock Exchange

Ms Selvarani Rasiah  
Legal Advisor, Listing, Kuala Lumpur Stock Exchange

Mr Inderjit Singh  
Listing Manager, Kuala Lumpur Stock Exchange

Ms Koay Lean Lee  
Senior Listing Officer, Kuala Lumpur Stock Exchange

Encik Nik Hassan bin Nik Mohd Amin  
Council Member, Association of Merchant Banks In Malaysia

Cik Zeti Marziana Mohamed  
Executive Secretary, Association of Merchant Banks in Malaysia

Ms Joanne Wong  
Manager, Association of Banks in Malaysia

Mr Lee Siang Chin  
Management Committee Member,  
Association of Stockbroking Companies Malaysia

Prof Abdul Manap Said  
Immediate Past President,  
The Malaysian Association of The Institute of Chartered Secretaries and Administrators

Mr Cheah Foo Seong  
Technical Director,  
The Malaysian Association of The Institute of Chartered Secretaries and Administrators

Mr Lee Leok Soon  
Technical Director, Malaysian Institute of Accountants

Encik Ali Abdul Kadir  
Vice President, The Malaysian Association of Certified Public Accountants

Encik Adnan Ariffin  
Executive Director, National Chamber of Commerce and Industry of Malaysia

Mr Chris Lee Wai Kit  
Manager, Ins., Mining & Services Rating, Rating Agency Malaysia Berhad

Puan Rohana Yusof  
Assistant Director, International Movement for a Just World

Mr Tommy Thomas  
Representating, Bar Council, Malaysia

Dr P.H.S. Lim  
President, Malaysian Investors Association

Cik Khadijah Abdullah  
Secretary, Federation of Public-Listed Companies Bhd

## APPENDIX 2

### MEMBERSHIP OF THE FINANCE COMMITTEE ON CORPORATE GOVERNANCE

Y Bhg Datuk Dr Aris bin Othman  
Secretary General of Treasury, Ministry of Finance - Chairman

Encik Ali Abdul Kadir  
Chairman, Securities Commission

Y Bhg Tan Sri Wan Azmi bin Wan Hamzah  
Chairman, Financial Reporting Foundation

Y M Dato' Raja Arshad Tun Uda  
Chairman, Malaysian Accounting Standards Board

Y Bhg Dato' Idrus bin Harun  
Registrar of Companies

Y Bhg Dato' Mohd Azlan bin Hashim  
Chairman, Kuala Lumpur Stock Exchange

Y Bhg Tan Sri Dato' Seri Ali Abul Hassan bin Sulaiman  
Governor, Bank Negara Malaysia

Y Bhg Tan Sri Azman bin Hashim  
Chairman, Association of Merchant Banks, Malaysia

Y Bhg Dato' Megat Najmuddin Megat Khas  
Chairman, Federation of Public-Listed Companies

Ms Wong Suan Lye  
Executive Director, Association of Banks, Malaysia

Ms Mohayani bt Shamsudin  
Chairman, Association of Stockbroking Companies, Malaysia

Prof Abdul Manap Said  
Immediate Past President,  
The Malaysian Association of The Institute of Chartered Secretaries and Administrators